PRIVATIZATION MANAGEMENT
TRENDS & PROSPECTS

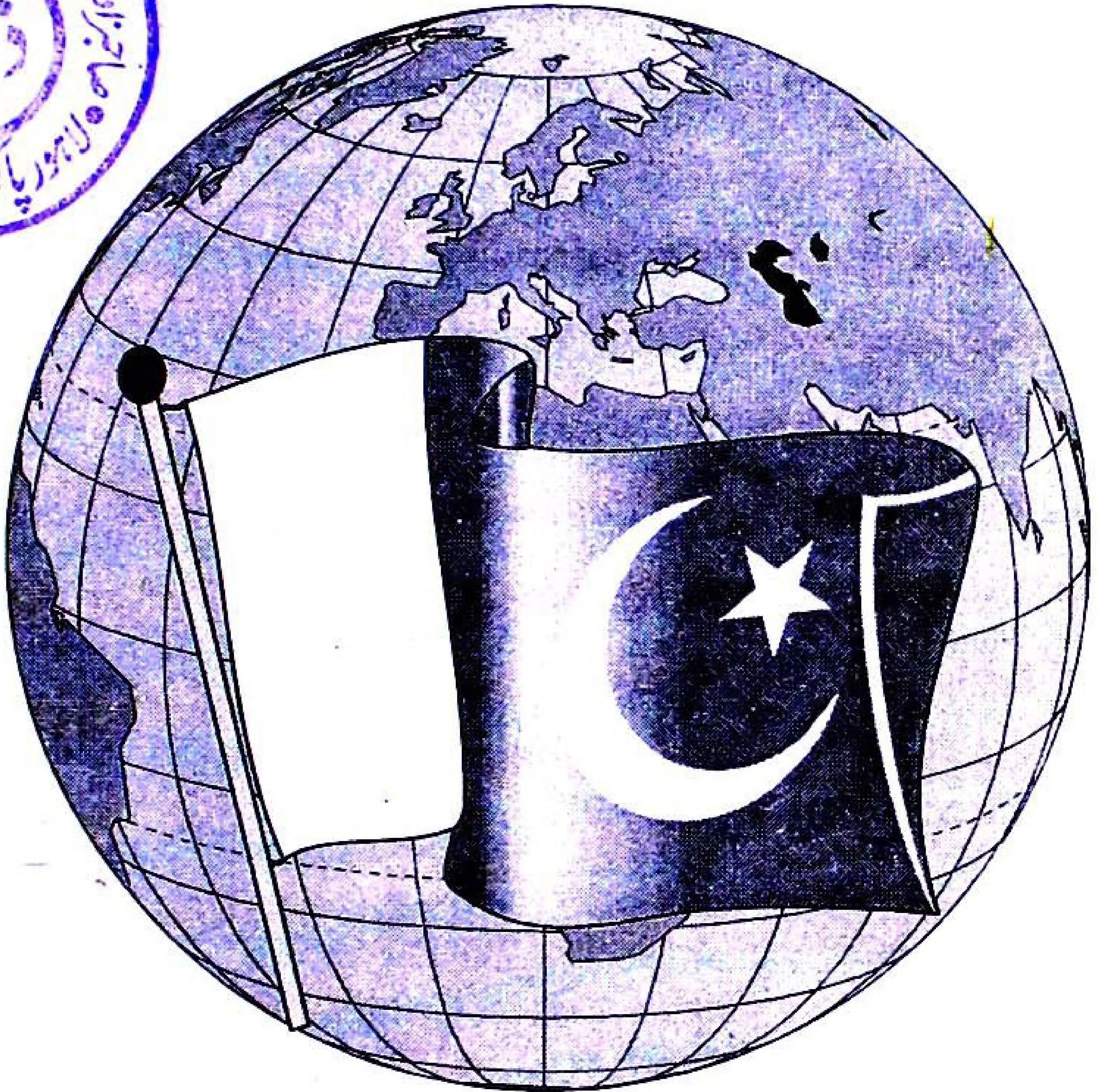


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PRIVATIZATION MANAGEMENT TRENDS & PROSPECTS





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IN THE NAME OF GOD, THE MOST MERCIFUL, THE MOST KIND

The Holy Verses:

To you O LORD, I offer my prayer; in you, my God, I trust. Save me from shame of defeat; don't let my enemies gloat at me!

(The Bible, Psalms:25.1–2.p550).

When comes the help of God and victory. (Sura CX:1)
Also corn with (its) leaves and stalk for fodder and sweet smelling plants. Then which of the favour of your Lord will ye deny?(Sura LV:12–13). So celebrate with praises the name of thy Lord, the Supreme

(The Qura'n, Sura V1:96).

Oh! Oh! Oh! how good is the Lord..
I never will forget what He has done for me.
He gives me blessings, how good is the Lord,..

(Anon, Hymn No 527:1–2)

WHAT WESTERN SCHOLOR SAID ABOUT THE AUTHOR AND HIS WORK

- "He has done Extremely well during his studies and shown excellent performance in viva voce examination. ......As his supervisor, I would note that his diligence and exemplary behaviour has made him an excellent ambassador for your University as well as Country and it has been a pleasure working with him."

Dr. Colin Mair,
Postgraduate Supervisor & Director SLAM center
University of Strathclyde Glasgow Scotland (U.K)

- "It was my pleasure to fulfil the role of external examiner of Dr. Sajid's Doctoral Thesis, I found him to be an extremely articulate candidate and well versed in his subject. His work indicates that he was very well focused on the task..... I feel sure that he will be a valued mamber of his profession and a recpacted researchor."

Professor Rechard Y Weaver
Chairman Department of Enterpreneurial Studies
Glasgow Caledonian University, Glasgow (U.K.).

DEDICATION:

EHSAN -UL-BARI MIRZA

&

MY HONOURABLE PARENTS

PREFACE

This piece of useful reading is designed for the benefit of all business executives, policy makers, economists, teachers and students of business studies. The academic material used in this book is arranged, organised and utilised mostly from the author's researech papers, riginal manuscripts and doctoral thesis on the privatization management.

Indeed, privatization has become a worldwide movement because of its popularity scale and scope in developed and developing countries. According to the latest data this wave of privatization is rapidly shifting towards the developing and Eastern European countries. It has been a part of broader experience aimed at liberalising the economy on several fronts; regulation, prices, trade and financial sector through the process of marketization.

Privatization as an instrument for economic development,is finding significant currency in developed and developing countries throughout the world. State owned enterprises(SOEs)'s poor profit performance discounted cash flow and heavy debt have raised many doubts about their economic efficiency in generating surplus capital for asian and third world countries. It is believed that privatization will yield a higher return on the capital invested which will accelerate socio-economic development. Due to social, political and economic gap between east and west, some of the policy makers are of the views that these western privatization models are not worth copying. However, like other developing countries, government of Pakistan has been pursuing the policy of privatization since late 1970s and early 1980s with a view to accelerating the pace of social and economic development and improving standard of living of the people. This privatization trend is now moving towards the major public utilities to prepare them for the sale or commercialization, in order to increaase the effeciency and effectiveness.

THE OBJECTIVES & STRUCTURE

The objective of this book is to provide first hand information about privatization trends at national and international level and also analyze the prospects of privatization for 21st century. The major focus is, the British privatization experience in general, and the telecom sector in particular, to learn the lessons from the worldwide privatization in order to develop a mixed model for implementation.

The book is divided into three sections, which are necessary in executing the structure of academic work. In order to develop and organise the background studies of worldwide experiences(DCs) and its lessons for LDCs. The formal structue is divided into three parts and each part consists of three chapters, these are as under:

PART ONE: WORLDWIDE TRENDS AND DEVELOPMENTS

First part starts with chapter one highlighting the movement of privatization from 'concept' to the world wide 'boom'. It is one of the rapidly growing movements in the world and equally popular in the capitalist and even in the socialist countries. Initially, this movement of privatization started in the developed countries but nowadays this wave of privatization has shifted towards the developing countries. Eastern Europe and Central Asia have now become the major centres of privatization activities and the major focus of the international donor agencies.

Chapter two, represents the major developing countries of various political and economic blocs and regions of the world. The privatization trend has reached the global proportions. The causes of this trend toward privatization are various and in many cases no doubt peculiar to individual countries. This country's experience shows that each country has different social, political and economic constraints and a special economic reforms and structural adjustment programmes are run under the supervision of the international agencies. Chapter three, describes the privatization

trends and developments in Pakistan since late 1970s. The Government of Pakistan has privatized about 75 state owned enterprises, and its privatization of public utilities programme is in the process which requires the most applicable options/modes for its implementation.

PART TWO : THE BRITISH EXPERIENCE AND LESSONS

Section two consists of three chapters which cover the historical trend and development of nationalization and privatization in the Great Britain and lessons for LDCs. Chapter four devotes to privatization movement in UK with reference to implementation process, cost and post privatization performance of the enterprises. The UK is the pioneer in introducing one of the largest privatization programmes and is a leading advisor and exporter of this idea to the rest of the world.

Chapter five looks at the British experience of utilities privatization i.e. British Telecom(BT), British Gas(BG), Electricity and Water which are highly popular and widely noted and imitated throughout the world. The privatization of utilities was started in a view to promote efficient allocation of available resources by encouraging competition, reducing cost and making the privatized utilities more responsive to consumer needs and welfare. Chapter six is divided into two parts to study the UK's regulatory system/price cap model and the USA's rate of return regulation for the utilities sectors. This chapter deals with a comparative analysis focusing on their issues and scopes of both country's regulatory models i.e. RPI - X and R:R regulation and draws the appropriate options and lessons for utilities privatization programme with particular reference to the telecommunication sector.

PART THREE: THE PAKISTAN CASE & PRIVATIZATION MODEL

This case study section comprises three chapters as well. Chapter seven discusses the Pakistan's privatization of the utilities. This chapter reviews the public utilities, especially the major candidate for privatization, the Pakistan Telecom Company limited (PTCL), and its historical, managerial and financial development to present the current status and position of the organization.

Chapter eight explores the alternative policy options for industrial sector in general and in particular for telecom sector, in the light of worldwide and the UK experiences. Every option is analyzed and discussed with reference to the relevant set of available privatization modes. Finally, in the light of the political, social and economic situation of the government of Pakistan and drawing lessons from developed as well as developing world. A "mix model" is developed for the PTCL in order to introduce a commercialization approach in four stages of its implementation over a specified period of time. At the end, a selection of additional research papers are presented/reprinted, with due acknowledgement of the co-authors, because time has proved that they are of enduring value and are as relevant today as they were initially written and published.

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Prof. Dr. Mushtaq A. Sajid
Date: October ,24, 1998.

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October, 24, 1998 (Dr. M. A. Sajid)

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TABLE OF ACRONYMS

AJ&K	Azad Jammu and Kashmir.
AT&T	American Telephone and Telegraph Co
BT	British Telecom plc
ADB	Asian Development Bank
BOO	Built owned and operate
BOT	Built owned and transfer
BLT	Built lease and transfer
CCOP	Cabinet Committee on Privatization
ESOP	Employees stock ownership plan
EAC	Expert Advisory Cell
ECPL	Exxon Chemicals Pakistan Limited
FYP	Five Years Plan of Pakistan
ITU	International Telecommunication Union
IJI	Islamic Jehmuri Ittehad(Democratic Alliance)
IJV	International Joint Venture
LATAs	Local Access and Transport Areas
LDCs	Less Developed Countries(LICs)
RBOCs	Regional Bell Operating Companies
SALs	Structural Adjustment Loans
SEALs	Sectoral Adjustment Loans
MAS	Malaysian Airline Service/Magt Accounting System
MMC	Monopolies and Mergers Commission
Offer	Office of electricity regulation
Oftel	Office of telecommunications (The regulator)
Ofwat	Office of Water Services (The regulator)
Ofgas	Office of Gas Supply (The regulator)
OECD	Org. of Econ. Co-operation & Development (DCs)
PERLs	Public Enterprise Reform Loans
PIA	Pakistan International Airlines
PPC	Pakistan Privatization Commission
PDA	Pakistan Democratic Alliance
PSDE	Pakistan Society of Development Economists
TALs	Technical Assistance Loans
TELMEX	Mexico's Main Telecom Operator

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PART 1

Privatization Concept & boom worldwide

CHAPTER ONE

THE PRIVATIZATION: CONCEPT TO WORLDWIDE BOOM

INTRODUCTION

The privatization of government owned enterprises is nowadays a large scale process for the transfer of state owned enterprises to the private sector. Privatization, as an instrument for development is finding significant currency in industrial and developing countries throughout the world and is one of the important components of socio-economic reform programmes being implemented around the world. The major aim of this policy is to reduce the drain on government resources, caused by the persistent losses of public enterprises, and to create greater opportunities for private investors to expand and modernize these enterprises with the aim of liberalising the economic environment for rapid industrialization.

Generally 'privatization' means a transfer of ownership from public to the private sector, or simply divestiture of state enterprises. But in a broader sense, it includes all measures which are directed at transforming a state-dominated economic structure to one where the private sector assumes a dominant economic role and economic decisions are based largely on market signals. In order to secure significant efficiency gains in output, it is thought that the private sector should be fully associated with all sectors of the economy such as manufacturing, banking, energy, transport, communication, health and education.

Privatization has been prescribed as a means of improving the efficiency, and hence profitability, of public enterprises. Their generally poor profit performance, poor discounted cash flow and heavy debt have raised many doubts about their economic

efficiency in generating surplus capital for Asian and third world countries. It is believed that the privatised firm will yield a higher return on capital invested and will thus accelerate economic progress. Privatization has generally meant much more than merely transferring assets to the private sector. It has been part of a broader experience aimed at establishing and liberalizing the economy on several fronts including regulation, prices, trade and the financial sector. Approximately ninety countries have engaged in some form of privatization affecting about 7,000 state–owned enterprises, either by selling them off or by deregulating agricultural and industrial sectors or by contracting out government services. The above figures do not include the Eastern and Central Europe denationalization of thousands of small public enterprises.

There have been various traditions of economic policy in the world including laissez–faire economics, Keynesianism, monetarism, nationalization and supply side economics. During late 1950s nationalization began to be fashionable and reached its peak in 1960s. During the 1970s privatization began to be discussed as a development which appealed to both developed and developing countries and was adopted in a variety of countries. Privatization embraces deregulation, denationalization, competitive tendering along with the introduction of private ownership and market arrangement in former socialist states. Since 1989, Eastern and Central Europe (ECE) became a central focus of privatization after the political revolution. In both capitalist and socialist states, it is thought that consumers are likely to benefit from the extension of market forces, enjoying more choices, better qualities, lower prices and greater efficiency (Hartely K et al 1991). Hence, privatization has appealed to the developed countries, the newly industrialized countries, the former socialist countries and the developing countries of the world. This experience shows that the privatization movement has become a global phenomenon; a tool for social and economic development; an alternative choice for

promoting productivity and efficiency and a way to industrialization and liberalization. The privatization process has some social goals and objectives as well, including the equitable distribution of income, wealth and other opportunities. Governments are trying to utilise the skills and experience of the private sector in trade and industry and hence to confine the business of government confined to administrative and social matters.

THE ORIGIN AND DEFINITION

The term "privatization" is believed to have originated with an American policy maker, Mr John Diebold, who claimed the invention of this terminology (privatization) during his campaign to remove a government-owned service in the United States of America from the public sector to the private sector(Lord King, 1987). According to The Economist 'It is possible, that the word "privatization" first appeared in print in The Economist just over 30 year ago. It was suggested by somebody now dead, who may have subconsciously pinched it from something published somewhere else' (January 3rd 1992, p17). The author did not mention the name of the creator of the world "privatization". But there is the possibility that the above-mentioned Mr. John Diebold may be the same person who originated this term.

Privatization is an umbrella term which is used to refer to a range of policy initiatives in different countries with different modes and motives. The word privatize itself simply means the opposite to nationalize, as transfer of ownership of state enterprises to the private sector. The words "privatize" and "privatization" appeared for the first time in Webster's New Collegiate Dictionary in 1983, where their recorded use is given as being in 1948. This indicates that term "privatization" did not appear in the dictionaries until the late 1970s.

The Fontana Dictionary of Modern Thought describes the concept of privatization as `the substitution of private for public ownership and supply of a good or service. Privatization of a good and service that can be supplied by the competitive market may allow prices and costs to be reduced and output increased. If the industry is a natural monopoly e.g. the telephone network, privatization will not result in a competitive market and Economic Regulation of the private industry is necessary. It may be possible to separate off a part of a publicly owned monopoly and privatize it to form a competitive market. For example the retailing of the telephone to the public could, perhaps, be made into a competitive market, but truly competitive markets in the supply of telephone lines and exchange are unlikely. Private ownership and interest in running of a privatized company may result in greater economic efficiency. However, privatization of the supply public goods is unlikely to be efficient. In the form of privatization where the state pays a private firm to provide a good or service there may be difficulties in defining the good or service adequately and monitoring the quality output supplied. The privatization of firm in the public sector is a source of revenue to the state, through state loses any future profits such firms would have made. Empirical studies have varied in their conclusion about economic efficiency of privatization, but they tend to suggest that for the cost and price reduction to be obtained requires the presence of competition' (p682).

Another account of the different meanings involved in privatisation is given in the following table:

PRIVATIZATION CONCEPTS & DEFINITION

Table: 1.1

1.	The sale of public companies and assets to private interests.
2.	Elimination of government control and involvement or the move from more to less intensive form of involvement.
3.	Imposition of "business-like" management on public sector (i.e. competition; PRP; short term contracts etc).
4.	Whole economy level : "liberalization", eg : Reduction of government spending as % GNP; Elimination of regulatory controls; Reduction of tariffs/subsides; Elimination of labour market rigidities; Encouragement of private sector/market led development; and Tax reform.

Source: Mr. C Mair (1993) SGBS distance learning notes.

The first definition of privatization is the popular concept of privatization as selling state-owned enterprises (SOEs) to private investors either individual or corporate. The British experience of public enterprises i.e. Rolls Royce, Amersham, Jaguar and utilities i.e. British Telecom, Water services, Electricity and British Gas are the best examples of this mode of privatization. Other modes and concepts are also being implemented worldwide and in the UK as well. Taken together, these sales were the major sources of revenue of about £77.4 billion gross between 1979 to 1991 (C. Mair, 1993). The above concepts and combination of elements have been adopted by both developed and developing countries, in the light of the Conservative government's policy in Britain.

Scott Thomas (1993) has also shown the variety of meanings attached to the

concept of privatization : privatization originally meant sale or liquidation of productive assets owned by the state. The concept has been broadened considerably in usage, especially in the context of post-communist economies. It can mean selling the business, too. It can mean selling, leasing or giving away some or all of the assets in the enterprise concerned to management and worker. It can mean retaining government ownership of a large minority interest. It can mean stripping away viable assets for sale or giveaway, and leaving behind for the state nonviable assets, along with non-performing loans and other liabilities. It can mean giving to all adult citizens, for free or the nominal fee, vouchers that can be used to bid for shares in public factories. It can mean hiring foreigners to run holding companies charged with administering public factories in blind trusts for those citizen-owners. It can mean providing public loans and grants to state-owned enterprises for investment that will "prepare" them for sale, or to write business plans for the same purpose. It can mean all these things, and still include the sale of the some factories to the highest bidders.

The terms "enterprise" and "privatization" are interrelated. The Concise Oxford English Dictionary defines the term "enterprise" as boldness or effort and readiness to undertake new venture with boldness and effort. The term "privatization" is defined as the advocacy by the state of the private enterprises or the policy and process of making private as opposed to public. The Oxford Dictionary definition shows enterprise to be related to attitudinal and cultural goals and privatization as the policy and process to achieve the goals.

Oliver Letwin (1988) has traced the private sector in Britain back to the sixteenth and seventeenth centuries and it existed in other countries at various times, the Russia Company founded in 1553 being an example. Joint stock companies also began to emerge and these arrangements gradually became a common method of

funding the voyages as exemplified by the East India Company which became a modern Company in the second half of the seventeenth century. The Bank of England was established as a private sector joint stock company issuing loans on behalf of the government, and in trading in government loan stock began in the early eighteenth century. London had its official stock exchange by 1773. With the introduction of the canals and railways the volume of private capital grew gradually and the modern concept of the private sector limited liability company was firmly established with the development of the Companies Act of 1862 which indicates the roots of private sector in the previous century.

Adam Smith, favoured the privatization of Crown Lands on the grounds that private ownership could improve and provide more productivity and efficiency. He believed that the sale of the Crown Lands would produce a very large amount of money which, if applied to the payment of the public debts, would deliver from mortgage much greater revenues than any other lands have ever afforded the Crown. Therefore, origin of private sector development may be traced back to Adam Smith's theories.

Alan R Waters (1985) argued that it is now clear that due to the nature of the ownership and, hence incentive, a state entity cannot be as efficient as a private entity in the production of the same output. He further argues that vigorous economic growth in the developing countries can only be achieved by the privatization of the public enterprises.

OWNERSHIP AND MARKET STRUCTURE

The majority of economists are agreed that ownership and efficiency are not interrelated. Efficiency depends upon competition, management and enterprise itself. According to Christos P and Clarke Thomas (1993) the justification and

ground for private ownership is given on the basis of three theories. First, the neo-classical theory, which suggests that communal ownership – lack of private property rights – will lead to dissipation. Second, the dispersed knowledge theory, which suggests that knowledge is widely dispersed and that the effective and efficient acquisition and utilization of knowledge can only be achieved through price signals provided by the markets. Due to the limited transferability of knowledge, the state is more ignorant in business than the private owner. Thirdly, the residual claimant theory, according to which, modern production is organized and controlled as team production which involves interdependence among the efforts and contribution of individual members of the team. This is also much in line with the property rights school.

Hartley and Porker (1991) developed an economic model in which improvement in economic performance depends on ownership, competition, and managerial freedom, and where the external and internal environments also play an important role in the productivity and efficiency of the business. This complex and interdependent issue indicated by the authors in the following two variable model:

OWNERSHIP AND MARKET STRUCTURE: A TAXONOMY

Table:1.2

MARKETS			
OWNERSHIP	Sector	Monopoly	Competitive
	Public	A	B
	Private	C	D

Source: Attiate ott and Keith H., 1991

This model attempts to shows the impact of ownership and market structure on economic performance and suggests the following hypotheses:

(a) D is superior to A, here "D" representing private ownership and a competitive market and "A" has public ownership and a monopolistic market.

(b) D is superior to C, because "C" represents a private monopolistic market. This reflects the standard economic view which favours a competitive market.

(c) D is equal to or superior to B. This suggests that in a competitive environment private enterprises are better than public enterprises.

(d) B is superior to A, because "B" is in the competitive market – reflects the role of competition.

(e) C is superior to A, reflecting in a non–competitive environment the policy role of a private capital market.

(f) B is superior, inferior or equal to C, depending on the ownership role and monopolistic position.

It is difficult to prove that private ownership is superior and guarantees better performance; but there is some evidence that private enterprises may perform better than public enterprises. One study analyzed the performance and characteristic of the SOEs which were the major basis for the privatization movement. This suggested that important characteristic of public enterprises were as follows:

Table: 1.3

– Poor financial performance, – Overstaffing and inefficiency, – Dependent on subsidies and unilateral budget transfers, – Poor export performance and quality of goods, – Exclusion of competitive imports, – Exclusion of domestic competitors, – Corruption and red tape.

The above were the major negative points and characteristics of majority of the state owned enterprises which favoured the privatization movement worldwide.

OBJECTIVES OF PRIVATIZATION

The literature review shows that privatization has as a major objective to develop the private sector and introduce regulatory reforms in the public sector in order to improve efficiency, generate revenue/profits, create employment opportunities, provide quality of services and develop capital markets. The majority of governments do not have a coherent set of objectives especially at the initial stages of their privatization process, including Britain. Globally, different government have different privatization goals and objectives, in connection with their social, economic and political agendas. One of the most important objectives of the privatizations worldwide was to reduce the pressure from budget deficits. Furthermore, many of the privatization programmes of the last decades were implemented to raise the efficiency and productivity of their economies and industries.

Notice had to be taken, too, of the international context. Barie Steven described the trend to globalization and intensifying international competition that: "By most measures, the 1980s was a decade of vigorous internationalization – of production, of markets, of competition – and growing economic, political and technological

interdependence. Trade expanded at much faster rate than output, and foreign direct investment surged strongly. Recent years have seen the emergence of larger markets and, in some sectors, the scale economies to be reaped have increased substantially. At the same time, development cost of new products and processes are soaring, and international competition has sharpened greatly. A key strategy of companies in responding to these changes has been to step up mergers and acquisitions (M&A) both at domestic, and perhaps more importantly, also at international level." (Barie S. 1992, p14). This indicates that a new approach is needed to face the competition created.

The objectives of privatization policy in the major developing countries are to reduce the burden on the government and to create greater opportunities for the private sector to expand and modernize these enterprises in the LDCs. This is with the aim of liberalising the economic environment for rapid industrialization, self–reliance and to accelerate the pace of economic development. In the developing countries different governments have different goals and objectives according to their political and economic circumstances. It has been suggested that privatization has been expected to fulfill the following objectives:

PRIVATIZATION OBJECTIVES IN BOTH WORLDS

Table:1.4

DEVELOPED COUNTRIES	DEVELOPING COUNTRIES
(a) Improve the efficiency of the hitherto publicly owned corporation and important sectors of the economy by restoring market discipline in certain key areas;	(a) To relieve budgeting stains on governments;
(b) To reduce state involvement in enterprise decision making and resolve the problems of management and control which so often beset relations with nationalized industries;	(b) Creating a liberal economic environment;
(c) Reduction of state financial burden and PSBR;	(c) To improve efficiency, productivity and profitability of the enterprises through competition and elimination of state interventions;
(d) Contribution to the development of the domestic financial market;	(d) To facilitate the access of private sector to financial resources;
(e) To gain the political advantage;	(e) Insulating economy from political interference;
(f) To handle inflation and growing unemployment;	(f) To broaden the capital market and widen indigenous ownership;
(g) Transfer ownership to citizens, and	(g) Releasing resources for social and physical infrastructure;
(h) Easing problems of public sector by weakening the public sector union.	(h) To create a more favourable environment for foreign investment;
	(i) To bring workers/employees into share ownership.

Source: Liebermann (1993) and Vicker & Yarrow (1988)

These lists of objectives indicate that the majority of goals of both developed and developing countries are the same. The major difference is that the industrialized countries depend on their owned internal resources to implement the privatization policy to achieve these objectives and the developing countries depend upon the international agencies to provide them with ideas and loans to implement the policy. The wave has been slowed down in the developed countries as the data shows, and accelerated in the developing countries including Eastern European countries. Their major goal is to transfer ownership and to create the environment in which a market economy can thrive. Some of these Eastern and Central European countries have achieved the transition process and other are developing a framework to achieve it.

MAJOR MODES OF PRIVATIZATION

A variety of modes and techniques are adopted in the developing and developed countries of the world to achieve the objectives mentioned above. As the major objectives of both developing and developed countries are the same, their modes seemed also similar irrespective of their social and economic position and the structure of their industries.

However, the developed and industrialized countries' privatization modes may not suit the developing countries due to their prevailing circumstances such as their social and economic infrastructure and the political system and situation. One set of modes suited to one country or region may not be a useful option to another country or region. Western Europe, Latin America, Eastern Europe, Asia, and Africa have quite different business, social, economic environment and culture. The various modes adopted in most privatization processes are as follows:

MAJOR MODES OF PRIVATIZATION

Table:1.5

(a)	Public Offering
(b)	Private Sale of Assets
(c)	Joint Ventures
(d)	Management Contract
(e)	Liquidation
(f)	BOO, BOT and BLT Schemes
(g)	Employees Stock Ownership Plan
(h)	Voucher System

Apart from this, about a dozen other related options and routes are available for deregulation and liberalization programmes which will be discussed in later chapters.

ECONOMIC PERFORMANCE OF PRIVATIZATION

One of the major objectives of privatization by any mode and in any region, is to increase the efficiency and profitability of enterprises. Only efficient utilization of resources can improve the productivity and profitability of industries which leads to economic development of the country. From the Second World War to the late seventies, the macroeconomic policy of the UK and some other countries was based on Keynesian economic theory, as one of the major aims of government was to maintain a high and stable level of employment. But policies changed with the passage of time and with the perceived failure of traditional Keynesian policies to

maintain full employment and inflation (Howard Vane 1992). Hutchison G. (1991) studied the economic performance of seventeen British companies and categorised them into five industries: Aerospace, Auto-making, Civil Aviation, Electronic and Electrical and Ground Freight. The success and performance programme was examined in the light of two hypotheses.

(1) The performance of privately owned enterprises is superior to public owned enterprises.

(2) The change in the British government in 1979 had a positive effect on the performance of the firms in the economy.

The analysis was done through comparative studies of public versus private enterprises, based on the descriptive statistics and general trends between ownership and performance over the entire sample. This research shows mixed results as to the effects of the ownership and performance of the firms. The publicly owned were found to correspond with higher growth in labour productivity and privately owned enterprises produced higher levels of profitability. The higher profitability leads to higher performance of the industry and economic growth in the country.

In 1992, the World Bank sponsored a research project of three regions, Europe, Latin America and Asia. The project involved case studies of twelve major privatized enterprises in the United Kingdom, Malaysia, Mexico and Chile. The results indicated that eleven out of twelve privatized enterprises improved domestic and world welfare and that productivity went up in nine enterprises and stayed stable in the other three. The workers' position remained the same and even improved in three cases, buyers made money and shareholders gained as well. As

a whole the privatized enterprises showed higher profits, faster growth and greater access to investment.

Another study, "Efficiency Gain from Privatization: An International Empirical Analysis" (Meggison et al 1992), took a sample of 41 organisations fully or partially privatized by share offerings in 15 countries including Mexico, Jamaica and Chile. These appeared to show substantial efficiency gains. The privatization of these state owned enterprises increased return on sales, improved internal efficiency and increased capital expenditures as a result of faster growth and high investment by better utilization of physical and human resources (Sunita Kikeri et al, 1992). These examples provide evidence that worldwide privatization is growing and mostly providing positive results in social and economic development.

The following table shows the scale of the privatization programme and proceeds during last decade in selected OECD countries:

THE SCALE OF PRIVATIZATION DURING 1979–1991

Table:1.6

OECD countries	privatization period	Accumulated privatization proceeds absolute	As % of average GDP over the privatization period
Austria	1987–1990	Sch 12.7 billion	0.9
Canada	1984–90	C$ 3.1 billion	0.6
France	1983–91	FF 82.4 billion	1.5
Germany, FR	1984–90	DM 9.7 billion	0.5
Italy	1983–91	L 13,500 Billion	1.4
Japan	1986–88	Y 11,000 billion	3.1
Netherlands	1987–91	FL 4.9 billion	1.0
New Zealand	1987–91	NZ$ 9.0 billion	14.1
Portugal	1989–91	ESc 364 billion	4.3
Spain	1986–90	Ptas 207 billion	0.5
Sweden	1987–90	SKr 14 Billion	1.2
Turkey	1988–91	TL 3,500 billion	1.6
UK	1979–91	44.5 billion	11.9
Source: National Westminster Bank Quarterly Review 1992			

The above table shows the accumulated privatization proceeds of selected Organization for Economic Co-operation and Development (OECD) countries from 1979–1991. Since this period of time many more privatization programmes have been implemented. The total scale of privatization in these OECD countries was estimated in 1991 at about £121 billion and most of this came from the UK and Japan with their combined total of 92 billion pounds (Pitels C and Clarke T, 1993). The privatization movement in the developing countries including Latin America

and Eastern and Central Europe, was also growing quickly. In 1992, Latin America accounted for 35% of the value of worldwide privatization, more than any other region, and this had grown from 6% in 1988. Privatization revenue has been generated in the following developing countries:

GROSS PROCEEDS FROM PRIVATIZATION (1980–91)

Table:1.7

Mexico	8,350 Million Dollars
Chile(Since 1973–91)	3,400 Million Dollars
Brazil	3,070 Million Dollars
Venezuela	2,000 Million Dollars
Argentina	1,500 Million Dollars
Jamaica	230 Million Dollars
Malaysia	185 Million Dollars

Source: Compiled from World Bank Publication – 1992

This example shows that the implementation of the privatization process is crowing rapidly throughout the world. Once privatization is completed, the privatized firms can improve and increase the sales, assets and equity by improving efficiency, capital structure and growth.

The privatization and deregulation policy is spreading worldwide. The number of state owned enterprises privatized in developing countries and developed countries are estimated at about 7,000, with 2,162 of these belonging to the developing countries of the world. More than 70% of the sales in developing countries were accounted for in Eastern Europe and Latin America as mentioned in the table

at page 20.

WORLDWIDE PRIVATIZATION

With the successful privatization measures in Japan, Korea and Britain the development strategies of governments and aid-giving agencies have increasingly focused on the privatization of public enterprises in Asian countries. Privatization has been prescribed as a method for improving efficiency and hence profitability, of public enterprises. Their generally poor profit performance or discounted cash flow and heavy debt have raised many doubts about their economic efficiency in generating surplus capital for Asian and third world countries. It is hoped that, once privatized, the firm will yield a higher return on capital invested and will thus accelerate economic progress.

Because public enterprises have not been generating the expected surplus many alternatives have been proposed to improve their profit performance. The alternatives range from using better management tools and methods to selling the organisations to private stockholders and thus turning public enterprises into private enterprises. Enterprises which have consistently been drain on the public purse and are also judged to have failed to meet societal objectives may simply be liquidated and closed down or sold. Internationally in the 1980s and 1990s transferring public enterprises to the private sector was an important government objective in both developed and developing countries of the world. In most of the countries it has meant much more than merely transferring the assets to the private sector. It has been part of a broader experience aimed at establishing and liberalizing the economy on several fronts including regulation, prices, trade and the financial sector. Governments have cautiously set out to redefine the economic role of the state. In 1988, Japan and Britain were dominant in the overall privatization process. During the last couple of years the privatization movement

has been growing fast not only in Europe but also in Latin America and Asia. The following table shows recent trends:

NEW DIRECTIONS IN PRIVATIZATION

Table:1.1

Worldwide Privatization by Value in 1988	Percentages	Regional Privatization by Value in 1992	Percentages
Japan	58%	Latin America	35%
Britain	12%	Eastern Europe	32%
Europe	11%	Asia	6%
Asia	8%	Western Europe	12%
Latin America	6%	Great Britain	2%
Others	5%	Others	3%

Source: The Economist August 21, 1993

The table shows that between 1988 and 1992 there was a significant change in the worldwide pattern of privatization. In 1988 Asia including Japan accounted for more than two third of proceeds from privatization. The sale of Japanese Nippon Telegraph and Telephone (NTT) made this contribution higher as it was one of the biggest telecommunication privatization in world (Economist, 1993). Latin America's share in world privatization was only 6% in 1988, but after five years it reached at 35%. Now Latin America and Eastern Europe share more than two thirds (67)% of the world privatization by value. This worldwide development and trend of privatization programmes during the last five years shows that the privatization process has developed and grown in these developing regions. Therefore, the pace of privatization movement seems to be moving towards the developing countries, and the majority of these developing countries are now in the process of privatizing their big industries and public utilities especially in Latin America and Asia.

THE ECONOMIC PHILOSOPHY OF PRIVATIZATION

Many enterprises and utilities were originally established by private entrepreneurs and were later nationalised. A wave of nationalisations took place after the Second World War, when socialism was at its zenith and when many countries decided to own and control major economic sectors for the welfare of the society as whole. The success and failure of this socialist movement is controversial but it is widely believed that these state owned enterprises turned into unproductive, unprofitable, in highly centralized organisations. In the early 1980s, Thatcher's government, believing in the inefficiency of state owned enterprises took the initiative to sell British public enterprises to private investors.

The philosophy behind this movement was that privately owned enterprises would be more efficient and productive than state owned companies and that prices of goods and services would decline and the general public would enjoy the benefits of privatization. The British government was a pioneer of this political and economic philosophy and liberalization of economy. This privatization movement was a very popular idea and was followed by many countries in the developed and developing parts of the world. During the 1980s this wave of privatization was at its peak in the developed countries, and then moved into the developing countries of Latin America and Asia. The developing countries have an important role in the global economy, accounting for 76% of world population and 31% of world trade. (Ravi Ramamurti, 1992). In the early 1990s, this movement captured Eastern and Central Europe, and privatization is now booming in this region where different social, economic, industrial structures and cultural environments exist and where different priorities and policies exist. Much of this move to privatisation is dictated or imposed by the international advisory and donor agencies.

Privatization was pursued by the developed countries because of economic crises,

higher budget deficits, the advancement of technology, the role of unions and an ideology of "people's capitalism". The developing world followed it for the above reasons, but also for reasons of money, employment, education, infrastructure, the stabilization of the economy and of government. The developed countries managed this process themselves, but the developing countries have to depend on international consultants and financial assistance.

In response to this market the World Bank and other agencies changed and restructured their policies and offered services tailored to the development of an international economic reform programme.

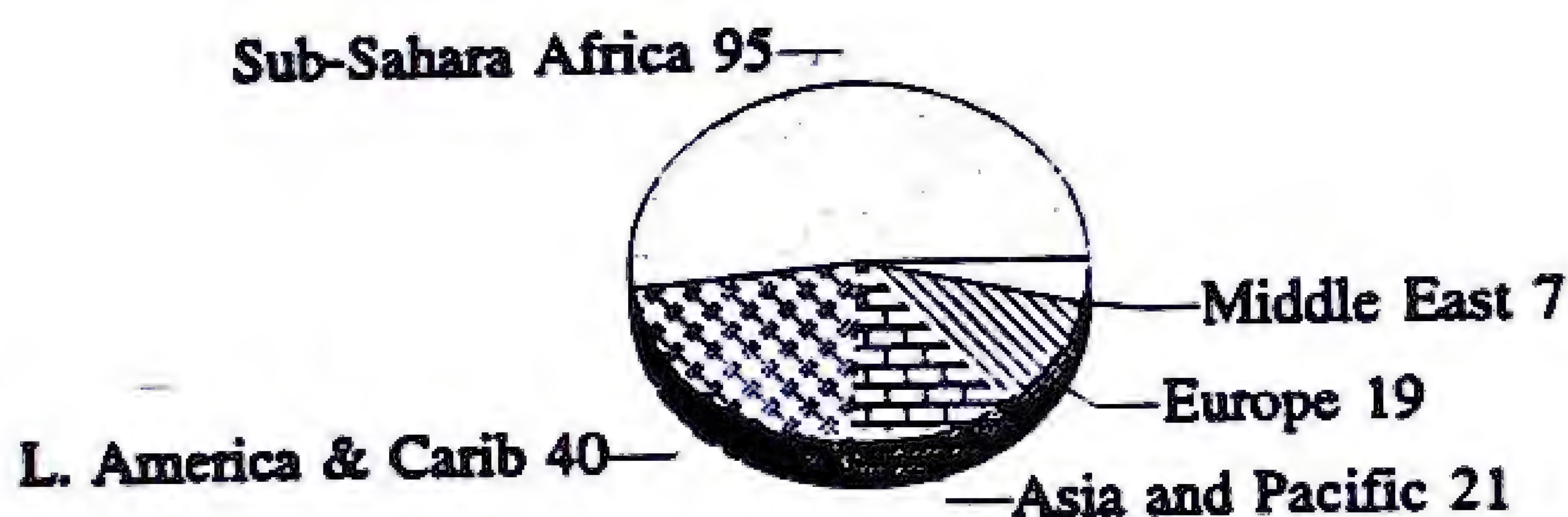
ROLE OF THE INTERNATIONAL AGENCIES

The World Bank lending programme for divesture started in 1981. The World Bank claimed that "sustainable poverty reduction is the overarching objective of the World Bank. It is the benchmark by which our performance as a development in the institution will be measured" (Sweeney Paul, 1992, p65). The institution faces basic questions of who will get financial assistance and how they qualify for it. The World Bank was influenced by the policy of Ronald Reagan and Mrs. Thatcher during the early 1980s. The World Bank administration decided that the market should be as free as possible. This became an official policy of the Bank with an "Action Programme" that the World Bank adopted as the blueprint to tackle poverty in the world. Since then, much of the World Bank's lending has been in the form of sector adjustment loans to European, Latin American, Asian, Middle Eastern and African countries. From 1981 to 1992 the World Bank supported more than 70 countries with 182 operations, the majority of them in Sub-Sarahan Africa, Latin America and Eastern Europe. Privatization has became an important part of the Structural Adjustment Programme (SAP) of the World Bank.

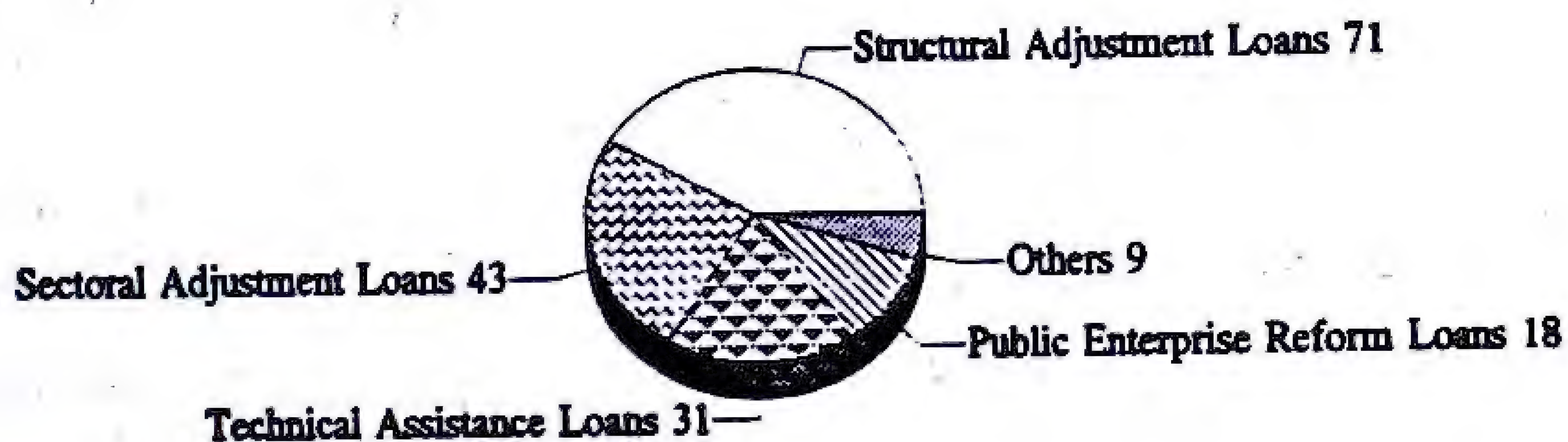
The world bank provides structural adjustment loans (SALs), sectoral adjustment loans (SECALs), technical assistance loans (TALs) and public enterprises reform loans (PERLs). During the last decade the bank has given these loans to the following developing countries of the world to develop and accelerate their privatization and structural adjustment programmes:

WORLD BANK SUPPORTED PRIVATIZATION IN DEVELOPING COUNTRIES, FISCAL 1981 THROUGH DECEMBER 1991

a : Numbers of Operations (Regions)



b : Numbers of Operations (Lending Instruments)



Source: Sunita, Nellis and Marry Shirley's 1992

The above data is for the year 1981 to 1992, where the World Bank supported 67 countries and 182 projects of Structural Adjustment Programmes in developing countries. The data shows that privatization has become an important part of structural adjustment programmes, through lending instruments/modes such as structural adjustment loans (SALs), sectoral adjustment loans (SECALs), technical assistance loans (TALs) and public enterprises reform loans (PERLs) etc. Apart from adjustment loans, about 60 Bank operations concern financial technical assistance for privatization in developing countries. Under these programmes the Bank supports preparation for privatization by providing financial and valuation advice as well as industrial and legal consultancy. The World Bank also has extended loans scheme programmes through two other branches or "windows", one is known as International Bank for Construction and Development (IBCD), and the other is the International Development Agency.

The other major international donor agencies are the International Monetary Fund (IMF), the US Agency for International Development (USAID), the International Finance Corporation(IFC) and the Asian Development Bank (ADB) etc. All these agencies encourage privatization programmes and are actively involved in financing, consultancy and advisory services to promote regulatory reform programmes. The World Bank used to be more concerned about the soundness of individual institutional projects during 1960s and 1970s, but it is now more concerned with economic reform programmes particularly in the context of Structural Adjustment Loans. Both major international agencies i.e. the IMF and the World Bank, have turned towards the development of privatization and this may have been due to the influence of conservative governments of in industrialised countries. The debt crises and fiscal pressure on the developing countries during the early 1980s made them dependent on these agencies for financial and technical assistance.

USAID IN PRIVATIZATION

The United States Agency for International Development (USAID) launched a private enterprise initiative in 1981 with the aim to promote economic growth in the developing countries. This USAID policy was based on the belief that private enterprises, operating in the competitive market would lead to broad-based and sustained economic growth. USAID realized in 1983, that "these approaches alone were not enough to turn the tide in LDCs. Capitalizing on world-wide trends to less government involvement and greater private entrepreneurship that were occurring, AID embarked upon a privatization initiative that enabled LDCS to broaden their efforts to promote economic growth. The Agency's privatization objectives was based upon the pragmatic realization that the entrepreneur and the competitive market are the most appropriate mechanisms for economic growth. A healthy independent private sector and secure individual economic freedoms also serve as a strong base from which to ensure the survival of democratic institutions' (Neal Zank, 1991, p175). Since then, privatization has become an integral part of the USAID's international development programme in the developing countries of the world. The Agency is engaged in providing various types assistance and support to the developing countries on changing the policy environment by funding the transfer of public assets to the private sector.

The Agency for International Development (AID) adopted different mechanisms and a variety of techniques to help the privatization programmes in LDCs. AID has been able to support countries like Bangladesh, Costa Rica, Gambia, Ghana, Honduras, Jamaica, Malawi, Mali, Senegal etc. to take important steps to promote and develop the privatization programmes.

In order to support the above countries USAID utilizes a combination of mechanisms which included:

(a) Economic Support Fund (ESF) to promote economic and political stability in the regions where US has special security and foreign policy interest;

(b) PL-480 was established to provide different food aid assistance to the LDCs and programmed in a way to help the agricultural policy reform efforts;

(c) Africa Economic Policy Reform Programme (AERP) was developed to assist the African countries who were willing to work on policy reform programmes;

(d) Commodity Import Programmes (CIPs) was started to encourage the policy changes and supply the industrial raw materials to local private industries;

(e) Project Level assistance and technical assistance are aimed at providing special training and reforms programmes to achieve the specific objectives within resources.

All these agencies and their sub-units are actively involved in encouraging governments of the developing countries to privatize their state owned enterprises and also to support the private sectors firms by providing necessary materials, finance and consultancy services.

When the role and direction of these donor agencies changed towards privatization, the privatization boom also shifted from the industrial countries to the developing

countries. Now more than 70% of world privatization programmes are implemented in the developing countries of the world and the major contribution is from Latin America and Eastern Europe.

A PRIVATIZATION BOOM IN FORMER SOCIALIST COUNTRIES

The economic and political revolution or conversion of Eastern and Central Europe and Soviet Union, since 1989, has given a new push for privatization. All the former socialist countries of Central and Eastern Europe are restoring and expanding private ownership and privatization. The process of privatization is involved in the permission and encouragement of private enterprises and ownership, and the sale of state assets to private companies and investors. The drive toward privatization in Central Asia and Eastern Europe has the same motives and basis as in Western Europe and rest of the world. The major reason for this development in the socialist countries is the expectation that privatization can raise efficiency and the standard of living through changed incentives (Mario Nuti D, 1993). Under the command economies of Eastern Europe and Central Asia state owned enterprises were inefficient and the production and quality of goods and services were poor.

Initially, these countries tried their best while employing various methods and reforms to improve their efficiency and productivity in order to compete in international export markets. But PEs could not produced any positive result in the shape of the efficiency and quality of services expected to them and these factors tended to worsen between 1970 and 1989 (Sunita et al, 1992). Comeron Colleen (1993) describes the reasons for privatization in mixed and planned countries by making a comparative analysis of the characteristics of a sample of 5 predominantly market countries – Canada, France, Italy, the UK, and the US – and 5 historically socially planned countries – Bulgaria, Czechoslovakia, Poland, the

USSR, and Yugoslavia – prior to the beginning of privatization. This revealed a common set of characteristics descriptive of all the countries in the sample. That set of characteristicswas then used to construct a model of the precondition for privatization in all countries. The common characteristic are:

1. sluggish growth in output,
2. accelerated inflation rate,
3. relatively the unemployment,
4. burdensome level of debt,
5. existence of a multiparty political system,
6. monopoly power in some industries and high cost of state owned enterprises,
7. subsidization of industries, and 8. strict control of the financial sector.

Therefore, privatization appeared to be derived from the social, economic and political situation of the countries. Apart from this there are specific arguments for privatization in these countries which are as follows:

1. A presumption and hope that privatization will inject life into the inert traditional system of the countries which was effected by the state ownership.

2. The privatization process is bound to reduce or weaken the opportunity for political interference in the economic life.

3. Privatization of enterprises and commercial banks together are bound to harden the 'soft' budget constraint of enterprises, and encourage the private

sector.

These were the main arguments which favoured the case for privatization, now occurring in traditional economies. Furthermore, the privatization movement developed also as the consequence of the resilience of private ownership in the socialist economies (Mario Nuti, 1993). Privatization is advancing in Western, Eastern and Central Europe as governments seek to reduce state supervision costs and spending on the deficit, raise revenue by selling state assets and improve the efficiency of operations by developing competition in privatized enterprises.

The privatization process in Eastern Europe is quite different from the rest of the world, because it is a more massive and complex undertaking. The collapse of communist regimes throughout Central and Eastern Europe and the destruction of the Berlin Wall has paved the way for the privatization of SOEs and assets on an unprecedented scale. For example, Romania, Czechoslovakia, Hungry and Poland announced thousands of enterprises for sale through the different modes of privatization. Hungary adopted management contracts, Romania and Poland sold through mass privatization whereas, in contrast, Czechoslovakia introduced voucher and coupon privatization.

The former socialist countries of Eastern Europe account for 37% of the sale of their larger and medium size enterprises. If one included the sale or liquidation of smaller enterprises such as the privatisation of shops, microenterprises, kiosks in the retail business and services etc, then the number would be much higher. According to one estimate, the combined sales of some selected Eastern Europe countries during 1992 were as follows:

EASTERN EUROPEAN MASS PRIVATION OF SOEs

Table:1.9

Poland	80,000 large and small enterprises
Former GDR	13,000 total large and small state enterprises
Czechoslovakia	7,000 total large and small state enterprises
Hungary	10,000 total large and small state enterprises

The rest of the countries also announced ambitious privatizing programmes and the implementation of these are in process with the help of international donors and consultancy agencies.

In the command economies, there is a feeling that privatization is "an end in itself" in that it is a major channel or tool to turn communism towards capitalism. On the other hand, under the mixed economies, privatization is seen as a tool to improve efficiency and productivity and to reduce the budget deficit, and it is not considered as an end in itself. (Sunita K. et al, 1992). In brief, at the end of the 1980s the dismissal of central planning in Eastern Europe led to an attempt to create a free economy by privatizing large sectors of their economies as the main solution to their problems.

Summing up, the different trends and highlights of the international experiencescan be listed as follows:

- Privatization is a political process and an economic development programme, which is growing throughout the world. This process required

an engineered and tailored policy package varying according to domestic political and economic circumstances.

- The privatization movement is moving to the Latin American, Eastern and Central European developing countries. Especially in the former socialist countries there is a requirement for a regulatory framework to support the privatization process and market-based economy.

- The international experience of Germany indicates that even under favourable financial, legal, political and technical conditions selling enterprises took some time.

- Successful privatization and industrial restructuring requires a healthy financial position and economic stabilization. The Eastern and Central European countries need a tailor-made privatization and denationalization policy and strategies consistent with the particular circumstances of their countries.

- Creating an appropriate framework of efficiency enhancement takes much more time and efforts than are usually envisaged at the outset of the reform programme. When governments make up their minds to move towards privatization, they almost always wish to strike hard and fast but they may not succeed as fast as they would like. All the successful privatizers of the developing and developed world's experiences emphasised that they designed and executed this policy very carefully and gradually.

- In Korea as well as in Singapore privatization as a policy was adopted, only after bringing most of the organisations to a high level of efficiency. The

privatization policy and restructuring is taking place in Vietnam, Hong Kong, Thailand, Indonesia, Sri-Lanka, India, Philippine, Turkey, Ghana and Kenya etc. The experience of these countries shows that the greatest opportunities for privatization are in services such as transportation, water provision, health care, education and telecommunication. The goals of privatization can be maximized when government ensures a competitive environment in the industrial and services sectors.

Finally, a literature review of the Asian, African, Latin American, Eastern European and other industrialized countries makes it clear that successful implementation of the privatization, deregulation and other economic reforms required full political commitment and a regulatory framework for the achievement of the desired results.

The next chapters will provide detailed studies of the privatization movement in selected developed countries i.e. the USA, the UK and selected developing countries from different parts of the world, including Asia, Bangladesh, India, Sri-Lanka and Malaysia, from Latin America, Chile and Mexico and some examples from the Eastern European countries and African countries as well, to explore trends and developments worldwide.

CHAPTER TWO

PRIVATIZATION EXPERIENCES IN DEVELOPING COUNTRIES

INTRODUCTION

This chapter is an analysis and overview of the recent trends and experiences of privatization in developing countries which provides some lessons for Pakistan's programme. Privatization with economic, social, political objectives and strategies is a relatively new experiment for the developing countries of the world. This wave of privatization is a response to the domestic economic and political situation of these countries. Developing countries have been adopting the privatization policy in one form or another since the early 1980s.

The privatization strategies, policies and programmes are as varied as the countries themselves reflecting the specific characteristics of their circumstances and their economic position. The developing countries set high goals for privatization e.g. the efficiencies of enterprises would be improved, capital market development would be stimulated, internal and external debt levels would be reduced, the allocation of different resources within the country would be improved, and there would be a greater attraction for overseas investment. There is a considerable debate about the fulfilment of these objectives and performance of the privatization programmes and its implementation. There is a need to make some observations about the developing countries to identify the trends and experiences during the last decade and the prospects for the 1990s. An important lesson to be be derived from the last decades is the heterogeneous nature of the implementation process of privatization in the developing countries. Because of the sectors and enterprises of different countries have their own unique characteristics that implementation strategies have to vary.

However, these countries have vast privatization programme in every field of enterprise. The recent trend of privatization of public utilities is increasing because the developing countries think that they have some good examples of privatization of public utilities from the developed countries for them to follow.

Privatization has been prescribed as a method for improving the operating efficiency and hence profitability of the public enterprises. Their generally poor profit performance or discounted cash flow and heavy debt has raised many doubts about their economic efficiency in generating surplus capital for the developing countries. It is often claimed that the privatised firm will yield a higher return on capital invested and will accelerate economic progress.

It is also claimed by some writers and economists that public enterprises are a drain on the public purse and have also failed to meet the social and political objectives set for them. As a result of this there has been growing criticism of public enterprises and their performance in some of these countries. Other policy makers argue that the main cause of poor performance of public enterprises and even of privatized ones in developing countries is poor planning and implementation. Wrong selection of product line, lack of qualified managers, underdevelopment of infrastructure and interference of the government in the management of enterprises are seen as the major causes of inefficiency. Nowadays the governments of the developing countries are gradually trying to eliminate these handicaps or weakness as a policy of learning by doing. Alan Rufus Waters states (1985) states that the present general downward trend in the economic performance of many of the developing countries and the existence of mass poverty, have increasingly led to the development of strategies of privatization; and foreign investment and private domestic capital are less likely to be regarded as an agents of foreign domination and exploitation. There has, therefore, been a willingness to look at alternative policies for the achievement of the

economic development through the reduction of government interference in the enterprises. Alan Waters also argues that economic theorv is now quite explicit and clear that due to the nature of ownership and hence incentive, a state entity can not be as efficient as private entity in the production of the same output.

For Waters economic growth in the developing countries can only be achieved through one solution; that is privatization of public enterprises. For him it is self evident that the managers of private enterprises have the incentive to work harder and manage better than the managers of the public enterprises. In the world Development Report (1983) Shirley suggests that public enterprises in Sub-Saharan Africa with the exception of those exporting minerals have become serious financial burdens for their countries. They have not been paying their taxes and most of their investment capital has come from government budgets. In some of the cases their cash surplus has been less than their depreciation and in a few enterprises their cash flow has not covered running costs.

The findings of Nellis J.R. (1990) also supported this view and concludes that

> *"few public enterprises generate revenue sufficient to cover operating costs, depreciation and financial charges; a good percentage do not cover operating cost alone. In many instances where Public Enterprises are classed as profitable, closer examination reveals distorted prices, direct subsidies, hidden transfers, preferential interest rates and a host of other elements which – if properly accounted for – would reduce the paper profit of the PEs in question. The conclusion is that African public enterprises present a depressing picture of inefficiency, losses, budgetary burdens, poor products and services, and minimal accomplishment of the non-commercial objectives so frequently used to excuse their poor performance ......"*
>
> *"Though every African country has one or more PEs which perform well by the most stringent of standards. on the whole public enterprise sectors are not fulfilling the goals set for them by African planners and leaders"* (Cook P.& Kirkpatrick Colin, P106).

The performance of public enterprises, in good times and bad times, on the whole, has been a burden on governments. In general, the overwhelming evidence from government's own reports, World Bank missions and scholarly studies clearly suggests that PEs have consumed far more resources than they have generated, and hence rather than contributing to national resources they have depleted them. However, these studies emphasise return on investment in financial terms, but it is difficult to measure all the non-financial, societal contributions which public enterprises can generate. Public enterprises which may have been making financial losses may have been effective in the use of its resources and yet show financial losses due to the cost of non profit goals imposed on it by government which were attained successfully. The state enterprises may have the responsibility of delivering services regardless of price, and state involvement in management and the burden of social responsibilities may result in a low financial rate of return on investment.

It has been suggested that in some developing countries, public enterprises have become a vehicle for corruption, nepotism, misappropriation of the public funds and indeed an instrument for furthering the political and material interests of the ruling parties. (Wilson Byernest 1986 & Berhuna 1988). Although these are very strong views these things are generally thought to have happened in situations where PEs experience substantial political bureaucratic interference in commercial decision making. The literature reviews show that the public sector enterprises have not been able to achieve their objectives especially in the developing countries. Under these circumstances, the privatization of public enterprises in the developing countries would be justified in order to dispose of the above mentioned problems.

Dennis A. Rondinelli (1991) also analyzed the rapidly increasing public debts, inadequate revenues and inefficiency of the SOEs in the developing countries by saying that "Inadequate revenues and high level of debt service exacerbate the

inability of the over-burdened government agencies to provide services and infrastructure efficiently. Many state owned enterprises (SOEs) in the public sector industry lose large amounts of money every year, further depleting the government treasury. SOEs account for a good deal of the external borrowing and absorb capital from financial markets that could be used by private investors to expand businesses that create jobs and increase tax revenues... The inefficiencies of many SOEs are clearly seen in their limited abilities to satisfy the rapidly growing need for services that are crucial for business expansion. Government owned telephone and telecommunications companies, for example, have been notoriously ineffective in meeting demand. The average waiting period for telephone installation in Indonesia is nearly 8 years and in the Philippines it is almost 7 years. In Thailand, customers must wait an average 3 years to receive telephone service. By 1989, the waiting list in Bangkok, alone had grown to more than 300,000 applicants. Moreover, even when telephone are installed, services remains poor" (Rondinelli D. 1991, p2). In addition to this evidence from Asian countries there is evidence that the efficiency performance in the Latin American and African countries is even weaker especially in the public service industries.

Colin Kirkpatrick (1989) discussed the fiscal impact of the public enterprise sector by concluding that

> *"The public enterprise sector in LDCs has failed to generate an investable surplus and instead has creates a budgetary burden for the public sector.. Employment opportunities have been lessened by the adoption of capital-intensive technology in production, improvement in employees' wages and employment conditions have created a privileged labour elite, subsidies on output have failed to reach the lowest income group thereby benefiting the better-off, and price controls on foodstuffs have disadvantaged poor rural producers. The*

empirical evidence appears to support the view that public enterprises have failed to realize their redistributional gouls, and, in some circumstances, have produced perverse results" (pp97–98).

Sunita Kikeri et al (1992) also expressed the similar view that *"evidence from a wide range of countries shows that far too many SOEs have been economically inefficient and have incurred heavy financial losses.. In many countries SOEs have become an unsustainable burden on the budget and banking system, absorbing scarce public resources"* (p15).

However, all the above mentioned problems are not attributable only to the state owned enterprises in developing countries; they can also be attributable to poor planning, faulty selection of product lines, underdeveloped infrastructure and undue interference by the governments. If all these handicaps can be removed and SOEs enjoy a competitive environment, then there is no reason that public enterprises can not be successful business entities (Berhanu Mengistu,1988). Mengistu's arguments seem logical, that if the governments in the developing countries can provide a free and competitive environment while commercializing the state enterprises, then SOEs have the ability to succeed and compete in domestic and international markets.

ROLE OF PUBLIC ENTERPRISES IN DEVELOPING COUNTRIES

No doubt, public sector enterprises are still powerful and dominant in most of the developing countries in certain fields of business and enjoy a monopoly position, because private sectors are not meeting the social goals of the governments, especially in the utilities sector. In the developing countries, the growth of the public sector during the past few decades was viewed as an important means of accelerating the pace of economic growth. This sector, in some countries, still accounts for a prominent share of total production and investment (Khawaja Sermand, 1991). Public

enterprises were established in these developing countries with the expectation that they would generate surplus capital and would also accomplish other societal, cultural and developmental objectives that were not necessarily financial in nature.

The private sector has different means and ends than the public sector. Private sector enterprises do not focus on providing the defined level of services because their primary objectives are financially oriented in order to earn maximum profits. Most public enterprises were designed for the purpose or objective of providing a specific good or service at a particular level and quality to a particular population. Providing the good and service was the enterprise's end and resources were simply the means to achieve that goal. Many enterprises addressed their economic and social purposes and a substantial number had managed to satisfy the requirement for which they were initially created. Some governments formed public enterprises with certain other additional socio-political objectives in their minds. Such objectives might include promoting industrialization, creating jobs, defending national interests, reducing regional differences and saving declining industries.

For the firms that were formed specifically to produce goods or services, the imposition of these additional goals was often incompatible with efficient market delivery of the required services and often led to poor financial performance. The state, through the responsible minister, should limit itself to giving a clear statement of objectives and terms of reference, and with the help of the board of directors to approve capital budgets, approve pricing policy, procure funds, review performance and also liquidate the enterprise when this is justified (Berhuwa J. 1988). The actual operation of the enterprise should be left to the discretion of its management and must be insulated from political interference so that the organisation can do its job and fulfil its objectives more efficiently.

Public enterprises are of growing importance in some countries because of the consequences of privatization which has not attained its appropriate objectives and efficiency. Public enterprises were often established and used as an instrument to create and preserve employment and to pursue social and economic development goals. In some developing countries much industrial employment was in the public sector. In Mexico, for example, the figure stood at 44%. The public sector has been an important instrument for the indigenisation of managerial level employees and an important forum for training managers. It is a high cost to public enterprises, but it is also to the long term benefit of the country. Similarly, in Senegal 70% of all managerial and technical personnel in the public sector were Senegalese against 32% in the private sector in 1977. This percentage of African managers in Tanzania, Kenya, Somalia, Egypt, Ghana is much higher than Senegal (Tony Killick, 1981). In 1987, the share of public enterprises in the employment of agricultural and related activities in Ethiopia consisted of 18.7% as against an estimated 76.6% of the total labour force engaged in the sector. The Ethiopian government service sector accounted for 46.3% and no less than 16% of the labour force and contributed about 38.6% to the GDP of the country. The industrial sector was dominated by PEs during and 1985–86 accounted for 96% of the gross value of medium and large scale enterprises, 95% of the value added, 93% of employment and 97% of fixed assets (Ameh E. 1992). These can be used as a counterweight to the concentration of private economic power and also to strengthen the economic position of a specific region of the country. In some cases, other non–economic considerations influenced the decision to reform or establish public enterprises to supply at subsidized prices as a means of assisting low income consumers, whereas the private sector can not do this. For this reason it has been said that PEs have been pursued for ideological and ethnic regions (Cook P. and Colin K. 1988). This mission of the public enterprises indicates that they are expected to assist in the solution of societal problems and are expected to be profitable as well. Such contributions cannot be measure in terms of financial

standards such as return on investment and discounted cash flow.

Obviously, it is inappropriate to measure the performance of state owned enterprises solely in terms of return oninvestment. While assessing performance the best way is to develop a criterion to consider profitability along with the societal contributions to the country. If these societal objectives can be calculated in terms of money or profits and if they fall short of the average industry level when compared with the private sector, then public enterprises become of dubious value and alternative strategies may be adopted (Berhawa J. 1988). In the developing countries public enterprises are highly concentrated in the public utilities, natural resources and also in the manufacturing sectors. The contribution of SOEs to the GDP in the developing countries rose from 7% at the beginning of the 1970s to 10% at the end of the decade. The public enterprise share of investment in total gross fixed capital formation exceeded 25% and in some cases accounted for more then 60% of investment. 65% of manufacturing value added is generated in public enterprises in Egypt, about 60% in Tunisia and 50% in Zambia.

A Latin American country, Brazil, registered 8.4 per cent growth during 1985. This growth was measured by the analysis of 100 state enterprises. The literature review shows that even in those countries where the total net profit has been unfavorable there are state enterprises with positive profit performance, e.g. Tanesco in Tanzania, Ethiopian Telecommunications in Ethiopia and KTDA in Kenya (Nellis V.W. 1983). One of the most important aspects of the success of public enterprises in some sectors is the impact they have on the national development. The real performance of public enterprises is difficult to measure as, whereas they ought to be subject to a process of performance evaluation, in practice there are considerable difficulties in making such an evaluation. Similar problems arise in the comparative measurement of the performance of public and private enterprises.

The performance of public enterprises can be seen to vary and, if one allows for non-commercial objectives, the trend may be on the positive side. For example, indigenous industrialization in developing countries is largely attributable to public enterprises and public manufacturing enterprises account for a relatively high proportion of the gross output of the value added in countries like Bangladesh, Egypt, India, Iraq, Yugoslavia and Syria (J A Ansari, 1981). There are some other benefits which are not shown when the profit performance of public enterprises is assessed, including decentralization in the location of the industries which can encourage the growth of the industries in all parts of the country. The introduction of new skills and technologies and the establishment of supply industries, in which private profit-oriented organisations can not invest, can secure the future development of the country. It is therefore difficult to say that the public enterprises are wholly successful or unsuccessful. As was mentioned earlier, it is easy to measure performance against financial objectives but it is much more difficult to measure the achievement of social and cultural goals which may be as important as other goals. Ideally, there should be a comparative evaluation of these goals between the public and private sectors, in order to help make decisions regarding development policy, but the measurement of performance against social goals is a complex and contestable concept. In the developed countries the analysis of the performance indicators in the 1980s was very much in terms of the three Es, although it is likely that there will be greater demand for the indicators of consumer satisfaction and quality during 1990s.

In fact, performance indicators are good tools for the measurement of performance, but the utilization of these tools in the developing countries needs to involve an adjustment to make them consistent with the specific characteristics of the developing countries to achieve the required results. The literature review shows that the experience of public enterprises in the developing countries has been uneven in

terms of success whatever criteria of success is used. This problem in the developing countries is the part of the planned development process of the countries, so there is a need to reorganize and develop the economic and social structure and organization cultures in those countries.

REASONS FOR PRIVATIZATION

It is difficult to specify the exact reason for privatization in each particular case. Some economists have related it to the political revolution and others have suggested economic reasons. Privatization in developed countries was motivated by political as well as economic reasons. Governments' commitments to lower taxes and reduce public sector borrowing requirements, was politically easier to achieve by selling government assets than by cutting public expenditure. On the other hand, for economic reasons they wanted to improve efficiency and productivity by introducing competition into the private sector. Additionally, the aim was to compete in a global economy where domestic SOEs were in a position to meet the requirements of the international market because of the quality of products and services and technological advancements. The need to achieve economies of scale which narrow home markets can no longer provide, for example, in the telecommunications and computer markets; the need to establish a presence in international markets; and the need to share rapidly–increasing R&D costs for the improvement and development of the quality of products, all of which present a serious challenge to public sector organizations.

There are political, historical and ideological reasons behind the privatization movement but economic factors probably lie at the root of all the reasons and explanations. For instance, change in political power may be due to change in the economic strength of various actors. The change in a country's official ideology may be the result of unsatisfactory economic performance under a previous ideology.

Governments of the developed and developing countries have faced large budget deficits, due to the oil crisis and debt crisis of the early 1980s. They found it difficult to arrange money from domestic and international sources to meet public sector requirements. Under these circumstances, privatization as a way of selling government asset to gain short term financial support was the alternative option.

Another important cause of the privatization movement is the international pressure from the donor agencies to pursue this policy as an economic reform programme (Ravi Ramamurti, 1992). According to Neal S. Zank (1991), besides the goal of efficiency, developing countries are pursuing privatization for a variety of reasons; for example, to generate immediate cash, to get foreign exchange and settle foreign debt, to improve the capital market and implement a free market philosophy and reduce their deficit by ending the costly subsidies of state owned enterprises. The economic and development case for privatization is based on three factors:

(1) public ownership is more extensive than can be justified in terms of the appropriate role of PEs in a mixed economy;

(2) the performance of PEs is poor compared to private enterprises;

(3) the inherent characteristic of public ownership is excessive state intervention.

Generally when public and private enterprises are compared in term of productivity and efficiency, the private enterprises are thought to outperform the public ones. Finally, it is also believed that the privatization movement is a reaction against the policy of nationalization and its impact on the economy of the affected countries, and privatization is being used to promote the idea of "people's capitalism".

THE IMPLEMENTATION PROGRAMME IN DEVELOPING COUNTRIES

The privatization programme was started in the developing countries by the influence of the developed countries and by the pressure of international donor agencies. The developing countries have various aims and objectives according to their social and economic positions. V.V. Ramandham has specified the broad objectives of privatization programmes in these countries as follows:

1. *To relieve the budgetary strains on the government:*
   - (a) *because of the loss of public enterprises;*
   - (b) *because of their investment requirement; and*
   - (c) *to permit the release of government funds for other uses.*

2. *To improve the efficiency of enterprise performance:*
   - (a) *through market disciplines and competition;*
   - (b) *by eliminating government intervention.*

3. *To improve allocative efficiency of investment:*
   - (a) *by improving the rate of saving and growth;*
   - (b) *by developing the money market.*

4. *To withdraw from the activities more suited to private enterprises, and where the original objectives of a public enterprise are fully achieved or are no longer valid so as to eliminate unfair competition with private enterprises.*

5. *To relieve the administrative burdens of the government.*

6. *To widen indigenous ownership:*
   - (a) *by encouraging a share-holding democracy;*
   - (b) *by making workers share-owners; and*
   - (c) *by raising productivity through stock-owning incentives.*

These are the major objectives in relation to privatisation of the developing countries of the world although some of them seem unclear about their priorities regarding these objectives. If this list incorporates a broad range of objectives of developing

countries, some vary from country to country. Furthermore, it is apparent that some of them appear to be in conflict with others, such as improving the rate of saving and growth at the same time as developing money markets; and also by encouraging a share-holding democracy. In the UK case, although primacy was given in government statements to the achievement of the economic goals of enhancing competition and efficiency, when these came into conflict with the immediate political objectives of quickly raising money by the sale of public assets, the political objectives were paramount. Its seems difficult to achieve all the objectives at the same time (David Marsh 1991). In the case of the developing countries, their major focus may be to generate cash to relieve the budgetary strain on government rather than introducing competition and developing infrastructure.

Few developing countries have a fully fledged organizational structure to develop a privatization framework under an independent institute such as a privatization commission. Privatization objectives are, therefore, often more theoretical notions rather than targets for practical implementations. Ideally, there should be a well defined organizational set up and structure within the government (like Pakistan's and Kenya's privatization commission) to permit orderly and efficient implementation including the prioritization of candidate enterprises, the definition of responsibilities of outside advisers, and the selection of advisors to monitor the implementation process. Most civil servants are not endowed with either the practical experience or the technical skills required in the implementation process. Hence, the implementation process has been very slow in some countries and very fast in the other. This has been the case not only in the developing countries but also in the developed countries. For example, in Britain with its expert advisers and attractive investment climate it took eight years to complete the first fourteen transactions and the pace was very slow in the initial years. Even now the process of privatising British Railways is taking a considerable amount of time.

Small sized enterprises can be privatized with relative ease, but there is a problem with larger enterprises because of economical, political and technical obstacles. Malaysia took three years to complete the privatization of the largest container terminal in the country. UBL, one of the commercial banks of Pakistan, is still in the implementation stage after three unsuccessful attempts in the last five years. In Mexico two attempts were made to privatize one of the largest copper companies over a span of two years and in the Philippines the government announced in 1987 its intention to privatize its National Airlines within sixty days but did not achieve this. These are a few examples which represent the complexity and difficulties entailed in the implementation of privatization programmes.

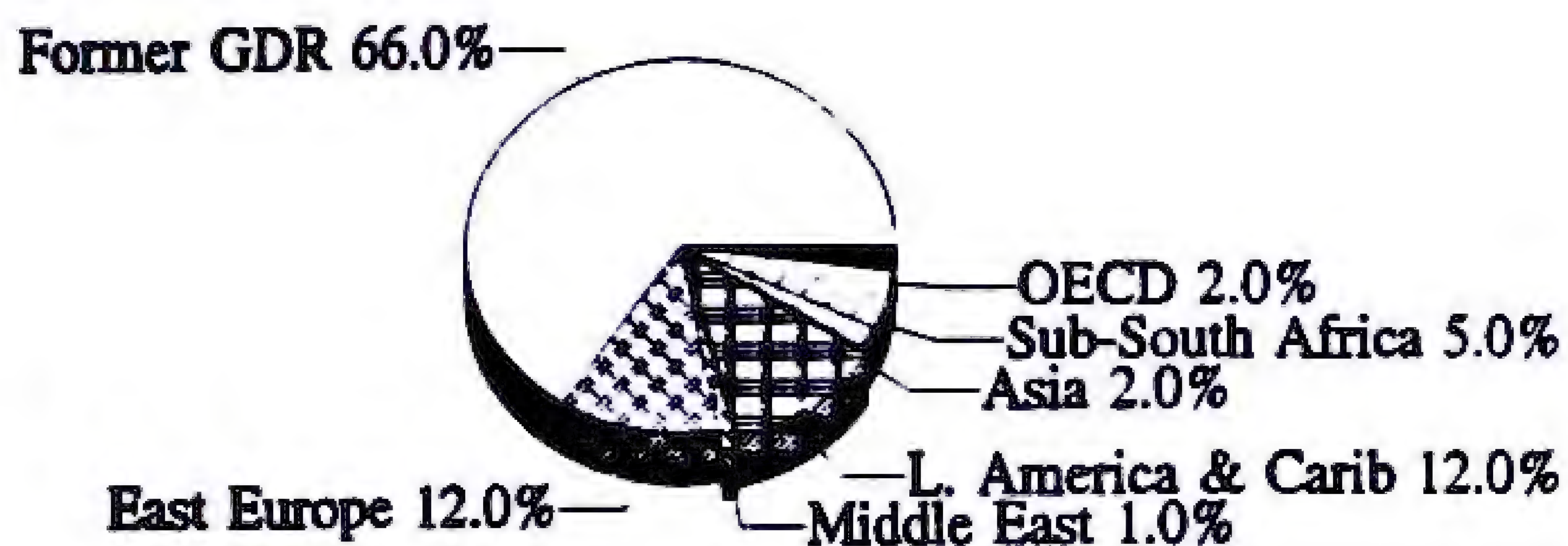
Although government has to be responsible for decisions about whether, what and when to privatise it must be recognised that these are complex and time–consuming decisions. Therefore, it is advisable for the government to hire private advice from lawyers, accountants, financial analysts, engineers and others who are professionally qualified for the job. Pricing play an important role and it requires a comprehensive analysis of the assets of an enterprise and then a determination of how the assets should be configured and valued to make them most attractive for prospective investors. This problem is particularly acute when there is a need for enterprises to be restructured prior to sale. Furthermore, each country has its own specific political and cultural environment which affect the implementation process in different ways.

According to Roger S Leads (1990) these characteristic of the privatization process, that is technical complexity and lack of uniformity, also suggest that policy makers and their advisers should lower their expectations in relation to the results of the process. Even if the momentum accelerates in the 1990s the pace of privatization in

most of the developing world is likely to continue to be sluggish, disjointed and tentative. Roger Leads further states that the experience of the past few years strongly suggests that the wave of privatization in the developing countries is not merely a fad that will soon pass out of fashion. The reason for this is that the main factors that motivate policy makers to consider privatization are as valid today as ten years ago. Khan and Reinhart prepared a research report based on data from 24 developing countries. The authors suggest that the arguments favouring the private sector in adjustment programmes have empirical support. They develop a simple growth model in which the effect of private and public investment on growth is separated. Comparison of the marginal productivity of the two types of investment allows them to conclude that "all in all, there does seem to be some merit in the key role assigned to private investment in the development process by supporters of market-based strategies " (World Development, 1990, p19). The authors argue that the policy to promote the private investment generally has significant benefits for long-run growth. The results of this simple growth model support the notion that private investment has longer direct effects on the growth than the public investment.

Private investment and deregulation policy is growing worldwide. The number of state owned enterprises privatized throughout the world is estimated at about 6,800, of which about 70% of sales were in the developed countries of the world, as is shown in the following table 2.1.

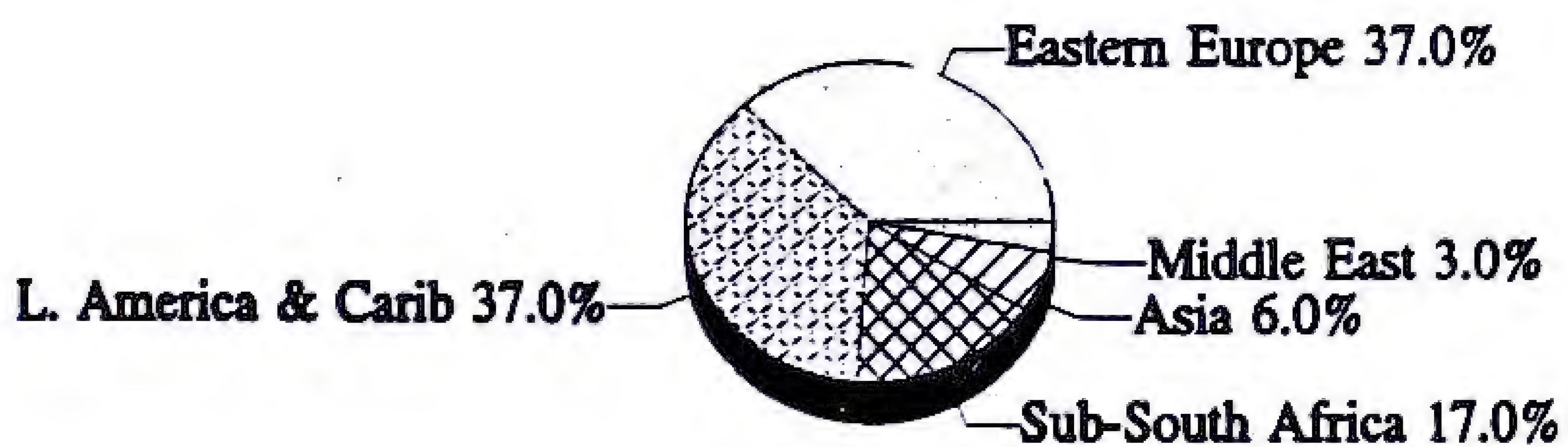
NUMBER OF SOEs PRIVATIZED 1980–1991



Source: World Bank Publication, Sunita et al, 1992

The number of public sector enterprises privatised in the developing countries in this period was 2,162 and their distribution in different regions was as follows:

SOEs PRIVATIZED IN DEVELOPING COUNTRIES, 1980–1991



Source: World Bank Publication, 1992

Since this period, the privatisation has continued apace. The Eastern and Central European (ECE) and Latin American countries are still maintaining their lead in privatization progress with the help of international agencies (see Appendix 2.1). In these countries the number of enterprises sold may be accounted for by mass privatization of small and meduim size units; but in terms of privatization by value/proceeds, the industrial countries are still holding the lead because of sale of the big business like telecommunications, airlines and other public utilities.

PRIVATIZATION: THE EXPERIENCE IN DIFFERENT COUNTRIES

A survey of privatization programmes of selected developing countries, conducted by Vernon W Heidi and H W Lawrence (1989), reported on the performance and problematic aspects of privatization programmes in these countries. The researchers found that there seemed to be little consistency across the countries in the nature of the candidates chosen for sale. But there appeared to be more consistency in the reasons for the selection of specific targets.

The general objectives in each country are to improve the performance of public enterprises. In a few cases, the privatization programme and its objectives are quite clear, but not in most cases. The analysis of the experience in most countries suggests that privatization is proceeding gradually, at best. However, almost all developing countries are divesting state owned enterprises. This wave of privatization in the developing countries is being done by offering shares publicly on the stock exchange, private sales of shares to domestic or foreign investors, management buy outs and the distribution of shares or vouchers to the general public.

The majority of the state owned enterprises have become financial loss makers because of the unique characteristics and problems of these developing countries. A typical example is the State Railway of Thailand (SRT) which took responsibility for

the operation of the country's entire rail network during the 1950s. With very little competition the SRT was initially profitable, but over the years it lost income joining the Bangkok Metropolitan Transit Authority to become one of the two largest loss makers among public enterprises in the Thailand during the 1980s (Levy and Menendez, 1990). In the public utilities, government-owned telephone and telecommunications companies have been shown to be inefficient in meeting demand in developing countries. Call completion rates are extremely low in many Asian and other developing countries because of faulty equipment and lack of switching capacity (Ambrosia and Chapon, 1990). It has been to the aim of improving these services and increase their efficiency that the sale of these public enterprises has been directed. Recent developments in privatisation in selected developing countries are now discussed.

BANGLADESH'S EXPERIENCE:

In the early 1970s, after independence, the Bangladesh government nationalized major industries. In July 1974, the government started considering liberalization of state industrial sectors due to the poor performance of the SOEs. By June 1982, a policy was announced to withdraw all restrictions on ceilings for private investment and only 6 industries were reserved for government ownership. This policy was revised in 1986 and again developed in 1991.

The shift to a policy of economic liberalization after 1975 has included some serious attempts to revive private investment through incentives and disinvestment by the government. Mr. Ershad's government was keen to promote manufacturing and pursued a policy reminiscent of early South Korea and Taiwan. While the industrial capitalist class in the country remains small and lacks of political influence, the government is nevertheless seriously committed to promoting industry, and this is potentially conducive to industrial growth (Clive Hamilton, 1987). The new

government has developed its own strategies and public enterprises are defined as public sector corporations and under each of them there are several other units. This sector now consists of 15 financial and 35 non-financial enterprises.

Privatization: What & How

The government of Bangladesh has divested a total of 1076 state owned enterprises including 609 in the industrial sector. Most of these divestitures took place during the early 1980s with 33 Jute and 27 textile mills returned to the former owners in 1982. The majority of these units have been transferred to the private sector or negotiated with the former owners and returned to them as part of the denationalization policy.

The government has also decided to carry on gradually the task of restructuring the equity base of state owned enterprises (SOEs) and has undertaken extensive rehabilitation of them. 49% shares of most of SOEs are being sold to private buyers as a part of the gradual privatization process and 15% of these have been given to the workers of the enterprises concerned. The USAID through the Centre for Privatization and the World Bank under the Structural Adjustment Programme (SAP) have helped the Bangladesh government and also carried out comprehensive privatization studies regarding the industrial and agricultural sectors. With the assistance of the above agencies the government made an evaluation of future privatization opportunities in the country and recommended appropriated strategies for the improvement of the privatization programme (Muhith A, 1989). The government has sold most of the manufacturing and agricultural enterprises to the private sector. For example, 50 enterprises under the Bangladesh Chemical Industries Corporation, consisting of 25 tanneries, 5 rubber plants, 7 manufacturing companies, 5 paper manufacturing units and 8 other were sold to the private sector through open bids, and in the Agricultural sector 30 enterprises which came under the Bangladesh Sugar and Food Industries Corporation were also sold to private buyers through open

tender for $11.5 million. The following industrial sectors were privatized in the following ways:

Agricultural (Food and Sugars mills), chemicals industries, textile and Jute mills through private sale; Iron and Steel companies by public shares; Machine Tools manufacturing unit through management contract.

Concluding Remarks

This privatization programme has been claimed as one of the largest privatization programmes in Asia and has been successful despite some difficulties at different stages of the process. However, the private investment trend is very low and has hardly improved efficiency except in the textile industries. As mentioned above majority of the state owned enterprises were sold under private sale, some of them through public shares and a few were privatized through management contracts. Seasonal floods, poor capital market and lack of international investment are the major problems for the public as well as the private sectors.

INDONESIA'S EXPERIENCE:

Initially, the Indonesian government's plan was to improve the efficiency and productivity of the state owned enterprises, because privatization was a controversial policy. Later, during 1980s, the government took the initiative to privatize loss–making enterprises. The inefficiency of the public enterprises caused the government to consider a privatization policy to decrease the deficits.

Indonesia has approximately 215 public enterprises with combined total assets of more than $68 billion that account for about 80% of the country's economic activity. These public sector enterprises covers every industrial sector, including the oil and

gas utilities, plantations, mining, manufacturing, textiles, construction and banking. The majority of the above mentioned industries were loss-making and for this reason the government decided to privatise in order to reduce the burden on the economy.

Privatization: What & How

The government of Indonesia has removed certain banking regulation and customs duties but has also decided to keep some of the strategic industries under its own control as the state bank controls nearly 77% of the financial sector. In Indonesia the ill-equipped stock exchange is a problem for the privatization process as in some other developing countries. There are about 24 companies listed, the combined market value of which is only $120 million, 1% of the government's annual economic output. USAID has opened a dialogue with the government on the benefits of privatization of the public sector and has provided technical and financial assistance to develop the privatization programme. As a result, the government decided to privatize some important enterprises as follows:

> Gaya Motor-car assembly, Kimla Forms-food and beverages companies were sold through public share offering; Gita Karya-printing and Perum Otorita (Engineering) were divested under private sale; Telecommunications and Mining were privatized through lease and BOT, BOO and BLT schemes.

Recently, the Postal and Telecommunications ministry has made a BOT agreement with 5 private companies to install 100,000 telephone lines in metropolitan Jakarta. These companies will install and manage the lines for 9 years, retaining 70% of the profits to recoup their investments. They will give 30% of the profits to the government and at the end of the agreement return the telecommunication system to

the Ministry of Postal and Telecommunication (Dennis A. Rondinell, 1991).

Concluding Remarks

The experience shows that the government is serious about the privatization and deregulation programme. The recent involvement of private companies in the postal and telecommunications sector will help the Indonesian government to double its base of telephone connections, by more than 2.5 million by 1995 and another five million lines will be installed by 2000 (Peter L Smith & G Stable, 1994). This Indonesian experience suggests that other governments, including the Government of Pakistan, should also take an interest in loss making enterprises as well and also adopt the BOO/BOT (built operate and transfer) schemes in order to accelerate development in the utilities sector. Experience suggests that under certain conditions private companies can play a valuable and cost-effective role in meeting growing demand. The Indonesian government moved gradually from industrial sectors to the big utilities such as airlines, shipping and telecommunication.

THE MALAYSIAN EXPERIENCE:

The Malaysian privatization programme was initiated by the Prime Minister Dr. Mahathir D Mohammed after coming to power in 1981. Dr. Mahathir took his ideas mainly from the UK as well as important concepts from Japan and organized a policy of "Malaysia Inc."

The Malaysian government's privatization programme represents a new approach to the development of the economy. The government has established a committee on privatization under the chairmanship of the Director-General of the Economic Planning Unit, established in 1985. The committee is responsible for the implementation of privatization policy. The Malaysian government has used its control over the public enterprises in order to reduce poverty.

The Malaysian privatization programmes and policies have made steady progress and achieved many of its major stated goals since 1983. The Privatization Master Plan of Malaysia has dynamic objectives stated in the "Privatization Handbook" of Malaysia which include:

(a) Relieve the financial and administrative burden of the government with respect to public enterprises;

(b) promote competition, improve efficiency, and increase the productivity of these enterprises;

(c) stimulate private entrepreneurship and investment in order to accelerate the rate of growth of the economy;

(d) assist in the reduction of the size of the public sector and its monopolistic and bureaucratic tendencies;

(e) contribute toward the objectives of the NEP (New Economic Policy), with particular attention to the role of Bumiputera entrepreneurship.

Privatization: What & How

The government has a huge privatization programme which is still in progress. Nearly 900 companies are under the control of government and the majority of them are supposed to divest to the private sector. These companies are from different sectors of the economy. The Malaysian government decided to privatize profit–

making as well as loss–making enterprises. The government has been offering some discount on the loss–making companies. More than seventy loss–making enterprises have been on offer and about sixty financially weak enterprises are in the process of sale and liquidation (Al Haj Soerno & Zainal Yusaf, 1985). In 1988, the government, with the help of the British government, started to formulate a master plan and feasibility study on privatization in order to accelerate the privatization process. Domestic and international consultants were involved in this study. The study included a survey of the full range of the public sector, and lays down a broad policy framework and guidelines for implementation of privatization programme. Programmes in progress include hotels, telecommunications, water supplies, shipping, national electricity, gas and the partial privatization of Malaysian Airlines System (MAS) in terms of the reduction of government ownership from 90% to 42%. The majority of the public flotations of the above mentioned large SOEs have represented only partial privatization. The methods employed for sale are quite varied i.e. private sale, public offering, private placement, joint venture, management contract, employee stock ownership plan, liquidation and the popular BOO/BOT schemes which are a major component of the Malaysian privatization programme. While employing various methods, some projects are completed and others are authorized for a combination of methods for future divestment.

Out of 37 existing projects 14 were privatized through the divesture of ownership via public and private placement, about 5 Malaysian style BOO/BOT schemes, 4 through management contracts and 2 projects via leasing schemes. The case of Port Klang, which is known by its new corporate name, Klang Terminal Container (KTC), is an interesting model involving a combination of methods, including an outright sale, a lease arrangement, an employee participation arrangement, and use of management contract. (M.L. Hensley and E White, 1993). Malaysian Airlines (MAS) did not see significant change in the operation of the company because of government policy and

its role in the enterprise. Similarly the aviation policy of the Malaysian container terminal at Port Klang could have been better handled because the government sold the profitable part of the port. The privatization of the terminal draws attention to the need for a careful redrawing of the boundaries between public and private ownership within the context of a carefully designed policy framework. Against a background of a declining percentage of foreign ownership and investment, the government is attempting to increase foreign investment by announcing a wide range of facilities and incentives. The government of Malaysia has used a variety of modes of privatization the sale of shares in Airline and Shipping Corporations, management contracting out in Construction and Telecommunications, and leasing BOO, BOT and BLT schemes in Shipping services and Telecommunications.

Concluding Remarks:

The Malaysian programme of privatization is one of the most rapidly growing and successful programmes in the developing world. The privatization programme has three unique characteristics. In the first place, it appears to be a more systematic and structured programme because it has established institutional and other administrative arrangements with the help of professional expertise and consultants. Secondly, the privatization programme enjoys a political commitment which is a good sign of its success. This plays a positive role in the development of the economy. Thirdly, the divestiture is taking place with a keen awareness of the possibility of a concentration of wealth and the need for ethnic balance (Nankani, H., 1990). Innovative techniques and a combination of different modes in the Malaysian privatization programme have helped in the expansion of infrastructure and of the public services and so is a useful model for the Pakistan privatization programme.

Malaysian's pioneering experience of the utilization of BOO/BOT techniques in a developing economy has provided a successful example of the mobilization and

utilization of private, domestic and international sectors. These schemes are utilized in the development of the social, political and economic position of the country, with the hope of turning its status towards 'Newly Industrialized Country' by end of the decade. The Malaysian Model provides a good and successful example for other developing countries of the world.

SRI LANKAN EXPERIENCE:

Sri Lankan economic reform started in 1955. The government made a long term plan in 1955 under Government Sponsor Corporation Act 1955, to divest and transfer the statutory bodies into joint stock companies. The 1957 Act permitted the government to take over all these joint stock companies. This process was accelerated during 1971 by nationalization of several key private sectors of the industries. The government established various forms of public enterprises, e.g. the public companies, government owned companies, the public corporations, government enterprises and government owned business undertakings.

In 1977, under the Land Reform Act, some further enterprises were nationalized which meant the country had one of the largest public sectors outside the centrally planned economies. The state owned enterprises (SOEs) accounted for around 40% of the gross output in manufacturing and over 40% of the employment in this sector. Out of 143 state owned enterprises, 127 were from non-financial enterprises and 16 from financial enterprises. They were performing below satisfactory level and so the government decided to improve their position and divest them.

Privatization: What & How

During the 1980s the trend towards privatization was started when a committee was appointed to restructure and improve the efficiency of public sector enterprises. In 1987, the World Bank gave conditional loans to the Sri Lankan government for the

divesture of state owned enterprises and corporations. As a result, the government formed a Presidential committee on the privatization in July 1987 which consisted of high level government officials and the private sector as well. The committee identified 18 enterprises which would be candidates for privatization. The Government has sold some of them and 11 enterprises have been partially divested and 5 enterprises have been contracted out to management (Nankani). The committee launched an extensive campaign to explain the objectives of the privatization programme along with the economic benefits.

The government endorsed the programme and objectives of the newly formed privatization commission. The rationale, criteria and merits of privatization have been debated and identified and three main techniques of privatization have been used by the government of Sri Lanka. The first complete ownership transfer has been used in the manufacturing sector, three textile factories have been sold to the private sector. At the time of sale these three factories were profit making units.

Second, partial ownership transfer. The government decided to convert the State Rubber Manufacturing Corporation (SRMC) in to a joint stock company, with 60% government ownership and 40% to be offered to the general public and employees. Initially the SRMC position was not good but after the formation of the new company its profits have improved.

Third, joint venture and management contract. This approach of full or partial privatization takes advantage of the greater scope for operational autonomy enjoyed by the joint stock companies relative to the public corporations. Under this mode the components of the Bank of Ceylon and Corporative Whole Establishment (CWE) were privatized.

Sri Lanka has had more experience with management contracts, because three textile companies, Thulhiriya, Pagoda and Veyangoda under the National Textile Corporation, Cement Corporation, Lanka Cement, Air Lanka and several Hotels were contracted out (Helon Nankani, 1989 and 1990). However, the Sri Lankan authorities have been careful in the choice of the instruments responding creatively to a multitude of environmental constraints. According to Peter Smith and G Staple (1994), "Sri Lanka has pursued a step by step sector reform program that has been strongly influenced by other commonwealth countries. The operator, Sri Lankan Telecom (SLT) has been corporatized, the scope for private investment has been broadened, and an independent regulator has been chartered, and all these steps have significantly increased the level and scope of available telecommunications. This is specially so for wireless services: there are now two cellular radio operators, and a third nationwide license is expected' (pxxi). This is a new development in the Sri Lankan telecommunications industry. Other industries like National Textile Corporation, Cement corporation and Air Lanka were privatized through management contracts and other manufacturing enterprises through private sale.

Concluding Remarks:

The Sri Lankan government experience suggests that the privatization of public utilities required reorganization before the implementation of the privatization process. Sri Lanka Telecommunication Department (SLTD) also provides a good example of the use of complementary sectoral policies in the case of public monopoly. Initial efforts involved formulation of the telecom policy framework, formation of a new legal entity and design of a regulatory body. Sri Lanka Telecom is also expecting to engage in joint venture programmes with Thailand and the Philippines. These Asian countries are paying more attention to the provision of utilities and the development of infrastructure in order to improve the social and economic position which is also a good sign for the economic development.

INDIAN EXPERIENCE:

The Indian government declared a privatization programme in the policy framework of its seventh Five Year Plan that commenced in 1985, while encouraging overseas investment in certain industries. The industrial policy assigns a more responsible role to the private sector which can operate in those areas which were closed to them e.g. telecommunications equipment, power generation and petro-chemicals. (Y. Venugopal, 1990). The Indian planning commission has outlined the eighth Five Year Plan, 1990 to 1995, which indicates the selling of 25 percent of state owned enterprises. It is estimated in the plan to raise Rs. 120 billion revenue for the government. According to the new Indian policy joint ventures are welcomed, with a maximum of 49 percent to be held by the government. The government has made further changes, easing the 40% ceiling on foreigners' equity holding in Indian companies, allowing Indian companies to raise equity capital abroad, revising monopoly regulation and raising the funds through the privatization programme (David Hourego, 1989, & K.K Sharma, 1988). The Indian government has made several plans with the help of the USAID but the implementation process is not as fast as in other countries.

The government has had to face different threats and strikes in the various industries along with political unrest (Kashmir & Punjab) and economy problems (poverty and population). However, the Indian public sector is very strong and accounts for 90% of the national income in banking, insurance, railways, telecommunication, mining, electricity, gas and water. Other important enterprises in this sector are forestry, transport and highways. This sector is growing in term of investment as out of every 100 companies 42 public enterprises have paid up capital of Rs 14,000 crores while other 58 private companies have paid up capital of Rs 1,200 crores.

Privatization: What & How

The Indian government policy involved, inter–alia, clements of deregulation, liberalization and autonomy to public enterprises in the seventh Five Year Plan, 1985–90. These measures introduced competitive elements into domestic industry and encouraged international direct access to the open market funds, redefining the role of public enterprises. The techniques of contracting out and franchising are not considered as privatization in India, only disinvestment, or divesture is considered as privatization. A greater role was given to the foreign joint venture programme in areas hitherto reserved for public enterprises. The Government of India is using a case by case approach to privatization.

Generally, privatization in India has the following policy and programme:

(a) case by case policy;
(b) deal initially only with loss–making enterprises;
(c) dealing with the competitive sector where the private sector is already dominant;
(d) includes conversion into joint venture of different sectors.

The Indian government has a great deal of social and equity issues along with those of financial and legal regularity. It is not clear that public enterprises can't improve or that the private sector can be more efficient through the simple transfer of ownership under the current situation. It would however, be unrealistic to proceed on assumption that the issue of privatization will not take an important place in future economic policy (Y. Venugopal, 1990). However, privatizations have been few, as far as central government enterprises are concerned, whereas state governments have more achievements than the central government.

Concluding Remarks:

The privatization process in India was started in order to improve the efficiency of the industrial sector and to reduce the government's financial problems. On the whole the privatization policy is slow–moving and public utilities have required a huge amount of investment in order to provide services to this highly populated country.

The Indian government can show good result if both central and states governments develop combined strategies and policies under a central committee (Ramanadham V. 1990). However, in India the pace of privatization and change in the economy depend on the stability of the government because government is facing other problems than the inefficiency of public sector enterprises. For example the burning question is the Kashmir issue which requires immediate attention and solution. Political instability in India is also a major cause of slowness of the privatization movement.

MEXICO'S EXPERIENCE:

Mexico is one of the largest developing countries in Latin America. Privatization and liberalization are growing fastest and most successfully in this region. Six years ago Latin America accounted for just 6% of world privatization by value. Since 1988, its growth went up to 35% of worldwide privatization, and sales of state owned enterprises account for 37% in the developing countries, more than any other region. Mexico and Chile made the bulk of their sales during the last decade.

Mr. Carlos Salinas, of the Institütional Revolutionary Party (PRI), which has ruled since 1929, took office as President of Mexico in 1988. He achieved tremendous progress by adopting various structural adjustment and economic reforms programme to boost the Mexico economy. The government succeeded in signing an accord

known as the North American Free Trade Agreement (NAFTA) which has important consequences not only for Mexico but also for the whole region. The Salinas government convinced the international world that Mexico now has a modern and stable economy, world class companies and is on the border of an economic miracle with the implementation of privatization and liberalization programmes (The Economist, 1993). Another sign of stabilization and a continuation of economic progress is the success of Salinas's colleague from the Institutional Revolutionary Party, Ernesto Zedillo as the new president of Mexico. His victory on August 21, 1994, is further strength to the economic development in the countries, but recently faced some temporary economic problems.

Privatization: What & How

The Mexican privatization programme is one of the most extensive and successful programmes in the world. In the early 1980s, the Mexican government was in an economic crisis. Due to a well designed and structured economic reform programme it is now the thirteenth economic power in the world and one of the major trading nations. The government reduced its state owned enterprises from 1,155 to only 220 between 1982 to 1992 and the rest of them are in the process of reorganization and restructuring. The privatization receipts in the order of 6.3% of GDP during early 1990s, were surpassed only by those in the UK and in New Zealand during their extensive privatization.

The Mexican government's privatization programme has the major objective of increasing economic efficiency and strengthening public finance. The government's policy is to close unprofitable plants and merge and privatize others. The privatization development programme was divided into three phases; initially small and unprofitable enterprises were either liquidated or merged from 1983 to 1985. The second phase, from 1986 to 1988, focused on selling mostly small and medium size

enterprises in order to get confidence and experience before tackling the larger enterprises and more complex transactions. This was Mexican government's strategy as put by Dr. Pedro Aspe, the Secretary of finance, "If one makes mistakes selling a night club or a bicycle factory... it is not as tragic as if these mistakes are made while selling the largest commercial bank in the country, the telephone company or a major airline" (Voljc Marko and Joost D., 1993, p132). The third phase was started from 1988 onward, after improvement of the macroeconomic environment and the development of confidence by starting from small enterprises. The guidelines issued in 1989 explained the procedure for domestic and foreign investments in different sectors. Some activities were reserved for state ownership i.e. oil and petrochemical, and other remained under the domain of Mexican citizens i.e. electronic media and roads.

Other areas were opened for international investors such as 30% investment in the commercial banks, 49% in insurance, fishery and telecommunication companies, 40% in car parts and secondary petrochemicals and 34% to 49% in the mining industries. However, in the case of majority participation a "trust" mechanism was created in some industries, for example, domestic air, gas distribution, mining, secondary petro chemicals, automobile parts and maritime transportation etc. to facilitate foreign investment and grant them the economic benefits of equity ownership but not voting rights (keeping golden shares). All other foreign investments are allowed although some require prior approval, especially more than US$ 100 million investments.

The government sold most industrial plants, mining enterprises, steel plants, and manufacturing firms during the third phase of privatization. In the utilities and service sectors, TELEMEX, Mexico Airline, Aro Mexico, Astilleros de Veracruz Shipyard, BABAMEX and 18 commercial banks were sold successfully. PEMEX,

one of the top three world class companies, will remain under state control, but it has been decided that the company can sign service contracts with private companies in order to expand and improve efficiency and productivity. This comprehensive privatization package has covered all fields in the economy including the industrial, financial, agricultural and utilities sectors. Private sector financing and construction is also established in the electricity, fertilizer and petrochemical industries. There are BOT schemes also in the infrastructure development and cogeneration and self generation of electricity plants.

According to Bazdresch P Carlos (1993) the privatization movement started in 1983, after a year of "debt crisis" in Mexico. The pace of privatization and economic reform programmes were accelerated since 1989. The annual GDP increased from about zero to around 4% and the target for 1994–1995 is 6%. The privatization programme has been successful through the liberalization of the economy, reduction of the SOEs, generation of revenue for the government, reduction of inflation (from 160% to 15%), and the stabilization of the economy. Most of these goals have been achieved and the evidence of the development shows that privatization has generated greater efficiency in the economy as whole during the last ten years.

Concluding Remarks:

These achievements suggest that it may be possible to secure a place for Mexico in the developed world, in future (Michael Marry, 1992). Mexico has made an unprecedented transition during a short period of time, with a successful privatization programme and a rapidly expanding role for the private sector. Mexico's well designed regulatory framework, adequate economic policy, full political commitment and gradual implementation programme provides a good lesson for other developing countries who desire to achieve the real benefits of privatization and the private sector.

CHILEAN EXPERIENCE:

The Chilean experience is another example of the most extensive experience of privatization in the developing world. It covers nearly every sector of enterprises from small to large corporations and banks. In 1973, the public sector had grown out of control, largely as a result of Allende's nationalization policy, and the role of the government was greatly extended.

In early 1974, the privatization programme began in the agricultural sector and covered the reprivatization of a significant portion of the land under the discipline of the market place. Nationalized banks were returned to the private sector. The retirement pension scheme hitherto financed through a distribution system was replaced by the privately capitalised social security financial societies. Moreover a land reform which had affected 43 percent of the country's cultivable area was rolled back by almost 40 percent. While data are weak, it is estimated that between 1973 and 1990 more than 400 enterprises were privatized, representing about 0.75% of GDP per annum. These efforts are judged as broadly successful, although there have been government reacquisitions of previously privatized enterprises, and policy reversals. Initially some phases of privatization were not properly managed because many enterprises were sold to groups with poor financial and management expertise. (H.B. Nankani, 90). The next phase of privatization was very carefully designed and planned and seemed more successful.

Privatization: What & How

In January 1983 a growing crisis in the domestic financial sector led the government to assume direct control over five major financial institutions of which two were privatized in 1986, one was merged with a private sector bank while the remaining ones were sold under the mechanism designed to promote what used to be called 'people's capitalism' through the provision of access to shares by small investors.

According to Ameha's report (1992) the following forms of privatization have taken place in Chile:

(a) direct sales of state owned enterprises most of them to foreigners;

(b) the sale of the majority state holdings and those in which a large minority stake had been disposed of including electricity generation, coal, sugar and telecommunication;

(c) all those enterprises which were in a poor financial situation and those that were bankrupted were dissolved and then put up for the sale;

(d) in some cases a certain amount of restructuring of the balance sheet of companies under liquidation took place by wiping out some debts;

(e) some companies were sold at auction or by competitive bidding although the law gave latitude for alternative arrangements with prospective buyers. The sales were open for national and overseas buyers and the sales price could be in local or foreign currency.

The scope of privatization in Chile has been extensive because it covers nationalized properties as well as small and very large corporations, banks, automobiles, fisheries and agro–industries. It also demonstrates that despite some setbacks, one can have a broadly based privatization programme through special incentives for small investors, employees, as well as large domestic and foreign investors.

Deregulation, liberalization and privatization have been the important elements in the economic policy of the Chilean government since 1973. The government has undergone four major phases of privatization: the initial attempt was made during 1973–1975, the second extensive programme was arranged during 1975–1979, the third, comprehensive privatization and reprivatization was attempted in 1984–1986, and fourth started from 1986 onwards, covering the remaining state enterprises. The Chilean government covered all sectors of the economy such as forestry, fishing, textiles, financial institutions, health insurance, and the major utilities. The privatization programme has been successful after some early problems.

THE EXPERIENCE OF CZECHOSLOVAKIA:

The privatization movement has different strategies in command and free market economies. Under the command economies, capital ownership is legally vested in the community. Practically, it means that ownership is in the hands of those who are enjoying political power; and controlled by planners and managers appointed by the power group. In debating the feasibilities of the planned economy Hayek and Mises argued that the modern economy consisted of thousands of enterprises, million of consumers and millions more products and services, and that attempting to plan for all this would be difficult if not impossible. Despite their predictions, the planned economy survived more than sixty years (Paul R. Gregory, 1990). The late 1980s and early 1990s saw the end of the Socialist planned economy and Eastern and Central European countries became testing laboratories for the rapid and comprehensive transition from communism and a centrally planned economy to democracy and capitalism.

Privatization policy was considered as an essential mechanism or tool in the successful transition to market oriented economies in the former communist countries. These countries wish to achieve the large scale privatisation of the state

owned enterprises as quickly as possible. This transition from one system to another required a time period and legal framework and the commitment of the governments. Within the last five years Eastern and Central European (ECE) countries have shown tremendous progress. For example, former Czechoslovakia, Hungary and Poland are quite successful and are providing models for others. Some other ECE countries are slow in this process because of lower foreign direct investments than required and expected for sustained growth (Anonymous, 1993). The above successful examples are those countries which have ties with the rich Western European governments and acquired their supervision and support for the development of the privatization process. Czechoslovakia is one of them and is a very active advertiser among the Eastern European block.

Privatization: What & How

The privatization process in Czechoslovakia is unique in a number of ways. First, its privatization movement started from one of the most tightly centralised command economies. 97% of output was in the public owned sector in 1986. Similar proportions of SOEs existed in Eastern Germany and the Soviet Union. These were the extreme examples. Second, as compared to other ECE countries except Eastern Germany, Czechoslovakia has the most developed economy and workforce. Third, it has relatively smaller foreign debts, lower unemployment (at about 2.3%) and, after deregulation, a lower inflation rate as well. All these historical factors have put Czechoslovakia in an advantageous position.

Czechoslovakia became a state after the First World War, and after the Second World War Slovakia became a separate state. The republic was reconstituted by the communist regime in 1948. Czechoslovakia's "Velvet revolution" of November 1989 was appreciated, politically and economically by the right wing. The major priority now of Czechoslovakia is the speed of privatization and its development as a method

for success in the future.

Break Up of Czechoslovakian Federation:

The Czechoslovakian Federation was dissolved and broken up in late 1992. On January 1st 1993 the two states became independent. According to Tom Whitehouse 'they have agreed that each republic should finance its own budget and have settled for the creation of a Czech–Slovak free trade zone. The two privatization minister, Lubomir Dolgos (Slovak) and Jiri Skalicky (Czech), have agreed that although the second wave of the privatization process will be split, the first wave currently under way will not be interrupted and Slovak investment in Czech companies and Czech investments in Slovak companies will not be affected. Teams of negotiators from both republics are dividing the old federation's property on the basis that what is in Slovakia is Slovak and what is the Czech land is Czech' (Whitehouse Tom, 1992, p168).

After this dissolution, the Czech republic moved rapidly to privatise its major SOEs. It started its massive privatization with certain priorities, such as, the rapid achievement of economic efficiency with the introduction of an appropriate price structure and the creation of broader ownership of the means of production. The Privatization Minister set the following specific criteria to achieve these privatization goals:

1. Appropriate involvement of foreign investors.
2. Future investment in various sectors
3. Commitment of companies and employees to economic development.

Slovakia also has its own Privatization Minister, but the republic has a different list of issues, such as a large number of inefficient enterprises without solvent customers,

13.7% unemployment, poor infrastructure, shortage of domestic capital and low foreign investment.

Two Waves of Privatization:

Privatization started in February, 1991, when every citizen over 18 could buy non-transferable vouchers points worth 1000 points to 1035 Crown and these could be used a variety of bids for enterprises. This scheme attracted the interest of the public and many people invested under this popular scheme (Pollat, A., 1993). Small factories, real estate and stores and hotels were sold during 1993. The Czech republic sold about 22,000 of these units and Slovakia sold 9,600 units. More than 100,000 small properties were returned to the former owners. Privatization of larger enterprises was divided into two waves. The first from 1990 to 1992, and the second 1992 to 1994. 62% of shares of state joint stock companies were slated for voucher privatization and the remainder were either sold to domestic or foreign buyers or kept in the hands of the Fund of National Property (FNP). The Czech Privatization Ministry transferred 1,872 approved projects to the FNP by the end of 1992. The second wave of privatization involved shares in 861 Czech companies valued at Kr155 billion. The Ministry of Privatization decided to offer coupon booklets to the Czech people for a nominal fee of CZK 1,050 ($36) and distributed these during 1993, and the second round of privatization through this scheme was started in early 1994.

Concluding Remarks:

Recently, the Slovak republic decided to modify and slow down the privatization process in order to increase its transparency and to improve its methods including participation of foreign investors by de-emphasising voucher privatization. The government identified over 600 State enterprises to sell through its specified methods

during 1994 and early 1995 (OECD Economic Survey, 1994). After the end of the Federation, the Czech Republic seems in a strong position politically and economically. The Czech government is enjoying a healthy budget, lower inflation, a strong balance of payment and lower unemployment than the Slovak Republic. For these reasons the Slovakian privatization process is slower than the Czech's overall and more complicated but successful.

NIGERIAN EXPERIENCE:

Since 1980, there has been a wave of change towards privatization and economic reforms in this region. Economic development theorists and international economists advised these governments to adopt market reform measures, in the hope that these economic policies and reforms could lead to better business performance and economic growth in the region.

Nigeria has a comparatively well developed capital market and started share dealings in the Lagos Stock Exchange in 1961. There are about 156 companies publicly quoted on Nigeria's six stock exchanges which are located at the major cities i.e. Lagos, Kaduna, Ibadan, Kano, Onitsh, Harcourt. A seventh exchange is planned at the new Nigerian capital Abuja (Guide to World Equities, 1993). According the above report, further deregulation of capital market has been slow due to a shift of responsibility for the pricing of new issues away from the Security and Exchange Commission to issuing houses themselves.

Privatization: What & How

The Nigerian government has pursued economic development programmes and a series of reform measures since independence 1960. The initial focus was on the development of public sectors and, since 1981, liberalising them. Nigeria is the tenth most populous country in the world and the fourth biggest oil producer in OPEC

having 68% of its revenues from it. They are called the giants of Africa and they believed that 'If Africa is ever going to produce a South Korea, they say it will happen in Nigeria' (The Economist, 1993 p49). But mostly they have been disappointed because of a lack of stability as is indicated by the existence of six military governments and two civil governments during the last 34 years.

The shift to privatization was started in 1981, when the Federal government established a Presidential Commission under the chairmanship of Mr. Onosode to examine and review the issues of state owned enterprises and the prospects of transferring them to the private sector. The commission recommended privatization of the public sector as a deliberate government policy for improving and inducing efficiency and productivity.

In 1984, the Federal military government set up a study group on statutory corporations and state owned enterprises in order to study the inefficiency of these enterprises. The study group was also responsible for examining the prospects for privatization of SOEs and the identification of appropriate candidates for divesture.

Major General Ibrahim Babangida came into power in 1985, and this policy took a new dimension. President Babangida was committed to privatization and commercialization policies. Under a law of July 1988 a Technical Committee on Privatization and Commercialization (TCPC) was established along with two sub-committees, one responsible for privatization and the for other commercialization. According to this privatization and commercialization plan all the state owned enterprises were classified into five categories:

(a) full privatization of public enterprises
(b) partial privatization of public enterprises

(c) full commercialisation

(d) partial commercialisation

(e) remain as public institutions.

The Nigerian government introduced two different terminologies, commercialization and privatization, the former referring to no practical divesture but the enterprise has to generate enough revenues to cover its expenditure without government support. Full privatization means that government will remove its control and ownership and hand over the state enterprise to the private sector.

The Nigerian government's structural adjustment programme which has been designed with the help of international agencies, consists of the major goals of the reduction of the burden imposed by the parastatals on the resources of the government and improvement of the efficiency of public enterprises. According to Ramandham, to achieve these goals through privatization and commercialization the government has the following objectives:

(i) to restructure and rationalize the public sector in order to lessen the dominance of unproductive investment in that sector;

(ii) to re-orientate the enterprise towards the new horizon of performance improvement and overall efficiency;

(iii) to ensure the positive return on public sector investment in commercialized enterprises;

(iv) to check the present absolute dependence on the treasury for funding by otherwise commercially oriented parastatals and so encourage their approach

to the Nigerian capital market;

(v) to initiate the process of gradual cession to the private sector of such public enterprises which by their nature and type of operation are best performed by the private sector.

The Economist (1993) reported that the Nigerian government had identified 111 state owned enterprises by June 1993 to offer for sale, and work had been completed on 88 units. This progress seemed encouraging except that the 111 left out all the important ones: Nitel (Telecommunication) NEPA (the electricity monopoly), NRC (Railway Corporation), NNPC (Newsprint Corporation), Nigeria Airways and Airport Authority. The government's privatization committee suggested partial commercialization (not divesture) in Railways, the Airports Authority, Electricity, Mining and River Authorities and full commercialization (moving towards privatization), for the Petroleum Corporation, Nigerian Telecom, Coal Corporation and Insurance Corporation. This suggests that the government is not keen to privatize these utilities and monopolies in the near future. The major cause of this slow movement is the instability and uncertainty of the federal government which has to coordinate about 30 local governments of different views and ideas as well.

Concluding Remarks:

A tide of economic reform programmes in developing countries of Asia, Latin America and Eastern and Central Europe, is in progress in African countries as well. This region is dominated by state owned enterprises, and these public enterprises present a depressing picture of inefficiency, huge losses, poor quality of goods and services and lack of managerial expertise. There is a clear need for proper planning, economic reforms and good financial management to overcome these problems.

Many other developing countries are also developing privatization programmes, such as the Philippines, Nepal, Morocco, Fiji, Turkey, Libya, Jordan, Egypt, Brazil, Ghana, Jordan and Tunisia and so on. All of these developing countries are directly or indirectly involved in privatization and economic reform programmes.

THE PROBLEMS OF PRIVATIZATION IN LDCs:

The problems of and obstacles to privatization arise from a number of social, political and economic factors. It is believed that privatization is associated with certain risks and limitations that developing countries' policy makers and economists should keep in mind before making their decisions. What is crucial here is the question of the organizational structures and procedures existing in developing countries. Because of this, in some cases the privatization process and programmes have been complex and ambiguous. As a result valuation problems are compounded in the developing countries.

In some countries neither the private sector nor the capital market is developed to yield even approximate valuation. Valuation of state enterprises took a great deal of time especially in Pakistan, the Philippines and Malaysia. Al Haj Soerno and Z A Yousaf (1985) describe how the Malaysian privatization was impeded by various administrative and legal constraints. Some departments operated under their own legislation that had to be amended through a long and complicated process in order to authorize them to sell off all or part of their assets. Some problems arose from the fact that all public employees had their pension rights constitutionally guaranteed by the government and as a result some alternative means of securing their pension had to be organized before the commencement of privatization. Claire Bolderson (1991) argues that the financial condition of these countries has also impeded the pace of privatization. Weak stock markets and low demand for shares slowed the process of privatization in Indonesia, India and Taiwan. Weak trading on the Jakarta stock

exchange and the tight money policies of the Indonesian government halted the privatization of state owned enterprises. Other examples of the problems are the street riots and political unrest which have occurred in Sudan, Egypt, Ghana, India, Zambia and Thailand. This has affected most of the political leaders, civil service employees and labour unions leaders who are afraid of losing their jobs (Financial Times, July 7). Stier K.J. (1990) says that strong opposition to privatization in Thailand has come not only from labour unions but also from the military because of their control over corporation and budgetary resources. In Pakistan the military is also not in favour of full privatization of the Pakistan Telecommunications Corporation for defensive and strategic reasons. W. Nicolas (1989) describes two main types of constraints which have consistently undermined privatization. These are implementation constraints which include technical constraints on implementation and are related to managerial and economic deficiencies. In some countries problems have emerged because of an absence of competent management consulting groups, accounting firms and investment banks to provide technical advice and to arbitrate between competing claims regarding the value of public enterprises being privatized. Once the public enterprise's assets have been evaluated by consultancy firms, administrative capacity is needed to examine buyers' bids, arrange finance and insurance as well as other legal issues regarding the privatization process.

Other problems include the following:

(1) Like all other economic reforms, privatization has distributional consequences and favours different groups within society at the expense of others. Its major impact is that it creates unemployment and encourages favouritism.

(2) If privatization has less effect on the pattern of relative price, then its macro-economic and distributional consequences are likely to be less tangible and

less important in scope and to create political problems. Some times it may undermine trade union power and might bring labour unrest.

(3) Some times ethnic conflicts disturbs the balance of economic and political power especially in countries with ethnic and religious distribution. Dennis Rondinelli (1991) argued that social, ethnic and religious groups benefitting from government control over economic activities, have also opposed the privatization programme in developing countries, especially in Malaysia and Indonesia where there is a general fear that privatization will give more control to the Chinese industrialists and the multinational groups or financiers. Malaysia's public sector was built as a counter–weight to Chinese economic predominance and to nurture a native Malay entrepreneurial class. Until that class has taken shape, privatization may have the effect of selling assets to the Chinese. In Kenya, the privatization policy is limited by the fact that the most likely purchasers would be Cacao or Asian business groups which would be politically unacceptable. The same problem occurs in the Cameroons and Pakistan that purchasing of the enterprises in done by selected dominant groups.

(4) Privatization reforms are more politically sensitive in those countries which have been following socialism or a nationalism that promotes a larger social redistribution in economic benefits. Sometimes it becomes a conflict between socialist and capitalist groups particularly in developing countries when they take their turn in power and do not accept the policies of the previous political group.

(5) Moses Kiggundu (1989) has noted that among the risks associated with privatization policy are those of political instability and the influence of

military.

(6) The social and economic limits and risks include the rising price of food, energy, water and transport as well as the threat of unemployment.

(7) The public sector bureaucracy is normally expected to play a leading role in the implementation of the policy. But in some countries the policy has faced resistance from within and has failed because of subtle opposition from public sector institutions. Such opposition may arise from the threat to personal benefits and may also be politically motivated.

(8) There is also resistance from economic groups who will be directly effected by the privatization programme. These may include current employees and the regional governments because of their regional interests and culture.

(9) The legal framework can create delays and problems before and after the privatization process. So the absence of an appropriate regulatory frame–work combined with investors' own preference towards the selection of new projects due to the advantages attached to them also constitutes one of the constraints.

(10) Another fear associated with privatization is that the private sector will eliminate services that are unprofitable. Alternatively that they will provide inferior quality goods and services to maximize their profits. Business will not be susceptible to control either by consumers or by public officials. As a result poor consumers will suffer.

(11) A common obstacle associated with privatization is the lack of trained and

experienced managers in the public sector. Their lack of experience and training makes it difficult for them to make the right decision at the right time about the right candidates for privatisation. This difficulty is exacerbated because they are attempting to sell loss–making enterprises which are unattractive to the private investors. Their lack of training also makes it difficult for them, once in the private sector to handle privatized enterprises.

(12) According to V.V. Ramandham (1990), one of the serious general problems in some developing countries concerns the civil and military disruptions in the political life, such as those in Bangladesh, Pakistan, Nigeria and Jordan. This adds to the problem of an already poor state of development of domestic financial markets.

CONCLUSION

The above study of the developing countries suggests that almost all these countries are in the process of privatization in one way or other. Rapid privatization is taking place especially in the utilities and services sectors i.e. telecommunication, electricity, transportation, water, education and health care. All these sectors are alleged to be poorly managed by governments which are not able to provide the good facilities and proper standards of service to all consumers. There is thought to be a need for private participation and investment in order to create a competitive environment for the improvement of services and life style leading towards the social, political and economic development of these countries.

The comparative study and literature review of this chapter shows that interest in privatization is growing rapidly in the developing world. This interest is encouraged by apparently successful privatization programmes in Britain, Japan, Korea and other developed countries, and also by international financial and aid–providing agencies

such as the World Bank, the IMF and USAID, which have enthusiastically focused on promoting privatization of public enterprises in the developing countries. As a result, almost every developing country is pursuing a liberalization and privatization policy to encourage the private sector and develop its economy. Privatization is occurring at a rapid rate in some developing countries, for example, in Malaysia, Mexico, Chile, Bangladesh and some Eastern European countries and at a slower elsewhere, such as in India, Jamaica and Kenya. For one reason or another the contributions of public sector enterprises to growth has been judged to be much below expectations and, in some cases, to be a fiscal burden on the economy. At the same time there is the notion that the private sector is much more efficient than the public sector. However, there is no guarantee that the private sector can produce efficiency and success and there are many unsuccessful examples to demonstrate this.

Experience shows that the problem is not one of ownership only. Often there is also a lack of a clear blueprint, organized planning, explicit goals, along with appropriate management control, motivation and reward systems and a suitable organizational culture. These "technical" difficulties may be as constraining as political factors. However, mostly privatization is a result of dissatisfaction with the performance of public enterprises, so the policies makers and development strategists argue that privatization can solve the problems and the latter may provide accordingly. However, reason suggests that the success of any particular privatization project will depend on other factors such as socio-political development, a well planned infrastructure and an appropriate implementation programme.

PART 2

Privatization Trends & development in Pakistan

CHAPTER THREE

PRIVATIZATION TRENDS AND DEVELOPMENTS IN PAKISTAN

INTRODUCTION

The government of Pakistan is pursuing a policy of privatization and deregulation as a key component of economic reform with a view to achieving economic, social and political development. Like other countries Pakistan's economic goals relate to increasing productivity and efficiency through more effective mobilization, distribution and utilization of available resources by private rather than public sector enterprises. Pakistan's privatization programme is one part of a major programme of economic development, covering all sectors of the economy to accelerate the pace of economic and social development and move towards greater self-reliance. It is based on the assumption that privatization offers the possibility of raising living standards by introducing competition which brings about efficiency, lower costs and better services.

Therefore, Pakistan has expressed its intention to privatize a large number of publicly owned and managed enterprises. The large and growing claims by public enterprises on national budgets with inadequate financial returns on investment, have been a matter of growing concern for governments in a number of developing countries including Pakistan. The reason for these increasing claims on the national exchequer have been two fold. On the one hand, the number and size of public enterprises continue to increase until the late 1970s. On the other, the less than satisfactory level of operational efficiency of these enterprises resulted in a continuous drain on the public budget. On both counts the aggregate requirement of the public enterprises increases to add demand on national resources. Until recently, investment

expenditure was considered synonymous with economic development and therefore the emphasis of the government has been on new investment with attention to operational efficiency either negligible or of secondary importance. Increasing constraints on government financial resources, partly because of operating deficits in public enterprises have now compelled the government to review public enterprises' operational performance and the substantial allocation of resources to this sector.

The estimated shares of the private and public sectors in real gross fixed capital formation during 1980 to 1990, indicates that the private sector has shown average annual growth rate of about 6.7% against the average of about 3.1 for the public sector. While the gross fixed capital formation in federal, provincial and local government has remained constant at about 20% of the total, the share of the private sector has increased from 45.3% in 1980–81 to 51.2% in 1989–90. The Auditor General office's report of 1989 shows the number of public enterprises had grown to 257 with assets of about Rs.276.7 billion. The annual report on government sponsored corporations shows 157 public enterprises which contributed 6.7% of the total GDP, but if the GDP contribution of Civil Aviation, Railway and Telecommunications, is taken into account then the share is 13 percent. The position of public enterprises in Pakistan, thus, does not appear to be excessive by international standards. The important element which influences public enterprise performance is government control of the prices of their inputs and outputs (Istaqbal Mehdi, 1991). The analysis of financial performance also shows a significant number of negative trends which are as follows:

(a) As the inflation rate in Pakistan is about 9% and the interest rate is around 15% enterprises generating less than this return on assets can be considered to be giving negative return on assets employed. There are only six

enterprises which are giving returns above 15% and only ten enterprises which give a return above 10%.

(b) Within the government sponsored corporations at least 51 units, with about 12% of total assets are incurring losses. In the manufacturing sector alone 5 units with about Rs. two billion assets were closed down because of losses.

(c) On the Karachi stock exchange in 1989, 356 companies were listed (now about 700) out of which 44 belonged to the public sector. These companies, with 56% share of total assets contributed 45% of the sales and generated only 38% net profits; their share in corporate tax was 37% and dividend at 35%.

The above figures would appear to corroborate the assumed effects of public ownership rather than the efficiency of public management. It is also consistent with the notion that generally public sector firms have higher cost structures. The conclusion of literature review as noted chapter 2 shows that majority of public enterprises especially in developing countries have not performed up to the expectation of their creators. Therefore, the government of Pakistan decided to adopt a privatization and deregulation policy to improve the performance and efficiency of the public sector.

THE DEVELOPMENT OF PAKISTAN'S ECONOMY

When Pakistan came into being on 14 August 1947, there were only 12 public enterprises, and government policy was in favour of private enterprise led growth. But rapidly, the need for public enterprises was argued in various sectors of the economy. In the beginning, public enterprises were created to supplement the activities of the private sector by filling the gap left by private entrepreneurial

activities. Later, a number of enterprises were created in the financial sector specifically to assist private sector activities and to accelerate their development role.

The pre-plan period (1947-55) was very important because the government was facing the problems of rehabilitation of incoming refugees from India. The government simultaneously attempted to provide a policy framework for the task of economic development. The most important step was the announcement of the industrial policy in 1948. In this industrial policy the major responsibility for investment was given to the private sector. The policy pointed out that 'Government is fully conscious of the fact that state action alone however beneficial or far-reaching, it may be, will not usher in an era of intensive industrialisation. Individual initiative and the private sector must play their part, if Pakistan is to succeed in building up a balanced economy' (Industrial Policy of 1948, p18). The industrial policy also envisaged that the government might find it necessary in the national interest, if private capital was not forthcoming in adequate measure for the development of any particular industry of national importance, to set up a limited number of standard units more as a means to attract private enterprise then any other object. Therefore the government was fully committed to provide all the facilities and infrastructure for achieving a 'healthy and balanced industrial economy'. The First Five Year Plan (1955-60) was actually released in 1957, when a planned development began in Pakistan. In the field of industry, during the first five year plan, the allocation to the public sector was 65% of total project investment. This plan was similar to the pre-plan period in the sense that the plan envisaged private enterprises as a main agent for the development and the public sector was expected to support it.

The plan stated 'private enterprise has demonstrated its ability to take up and accomplish new tasks with skill and vigour. We believed that in the immediate future

private enterprise, if fully supported and properly guided, can perform even greater tasks. The public agencies will have large and growing responsibilities of their own and the assignment to them of tasks which can be successfully accomplished by private enterprises will restrict the pace of development. The public agencies should concentrate upon their large and varied tasks and in the field open to private enterprises operate only in those geographical areas or sectors of development where the private sector lags' (First Plan, P85). Pakistani businessmen were largely concerned with land management, construction, trade and commerce. Existing private enterprise was not attracted to some industries because of their complexity, high investment requirement and relatively low profitability. The plan admitted 'some geographical areas are unattractive for lack of facilities. This together with the risk involved in launching new enterprises in untried fields have forced the government to undertake through the Pakistan industrial development corporation, industrial project in these areas where private business is unwilling to venture. It is however the announced policy of the government that enterprises built by PIDC should be transferred to private hands as soon as they have been established as going concerns and willing buyers are found'. In short, public involvement through P.I.D.C. (Pakistan Industrial Development Corporation) was viewed as transitional and time limited.

The Second Five Year Plan (1960–65) was committed to the liberalization ; which was sponsored and nurtured through government policy for promoting it. The strategy of this second five year plan was to continue to build and strengthen the existing institutions for credit, physical infrastructure and wherever possible those concerned with the social infrastructure. In the industrial sector, the government continued to restrict public sector investment to those sectors which were considered essential for development or security and for which private capital was not forthcoming. In respect of the private sector it was the capability and readiness of

private sector enterprises which was to determine the limits of their activities. In this plan, a number of steps such as the operation of an investment promotion bureau, publication of an investment schedule, nationalisation of industrial investment procedures import liberalisation etc., were introduced to favour the private sector and facilitate increased investment in this sector; the share of public investment was reduced by 15% in comparison to the previous plan.

The Third Five Year Plan (1965–70) also showed continued inclination towards the private enterprises, although the role of public enterprises was considered critical for various socio–economic objectives. In this period the public sector involvement was principally directed to building infrastructure and the provision of essential services in all sectors of the economy, especially agriculture and industry. Investment where capital requirements were large and the technology was complicated, or where private capital was underdeveloped were also foreseen.

The government was responsible for providing modern inputs in areas such as development in railways, roads and communication. In finance it strengthened and expanded operations to provide subsidised credit through enterprises such as the Industrial Development Bank of Pakistan and the Pakistan Industrial Credit & Investment Corporation. The role of the public sector was also emphasised in bringing about the reduction of disparities in the regional distribution of the resources (Mahsud A. 1990). Public enterprises such as the Pakistan Industrial Development Corporation were expected to establish a base for the capital goods industry and to act as instruments for import substitution. The Fourth Five Year Plan was not developed during the early 1970s due to the India–Pakistan war and the existence of martial law and other disruptions.

THE NATIONALIZATION PROGRAMME: EARLY 1970S

When the Pakistan Peoples Party (PPP) led by the late Mr. Zulfiqar Ali Bhutto came into power in December 1971, the government introduced a vast nationalization programme on the grounds of the unsatisfactory progress of private enterprise. The manifesto of the Peoples Party envisaged the role of the public sector as a critical instrument for controlling the "commanding heights" of the economy. The government extended the role of the public sector by introducing a series of nationalization measures. The manufacturing industries were nationalized by the President and the Chief Martial Law Administrator promulgated the Economic Reform Ordinance in January 1972, taking over management and control of 10 categories of heavy engineering, heavy electrical, assembly and manufacturing of motor vehicles, assembly and manufacturing of tractor, heavy and basic chemicals, petro–chemical, cement and public utilities i.e. electricity, gas and oil refineries. All 32 industrial units in these categories were taken over.

In March 1972 the government, in a second phase took over 32 life insurance companies and placed them under the control of the life insurance board which was succeeded by the State Life Insurance of Pakistan in November 1972. The Presidential order number 10 of 1972 explained this measure as aimed at 'the removing the interlocking of life insurance with private ownership of major industrial groups, extending the areas of operation of life insurance from the hitherto comparatively more affluent sections of society to the common man, increasing the return to the policy holders and providing cheaper and more economic insurance' (Pakistan Economic Survey 1973–1974, p9). Nationalization of Vegetable Ghee Industry took place in September 1973, and the Hydrogenated Vegetable Oil Industry Act 1973 nationalized 26 private sector enterprises. According to the charter of the Ghee Industry regulatory controls were needed in order to maintain the stability of prices and continuation of supply of this essential commodity. The hydrogenated

vegetable oil industry (HVOI), Act 1973 argued for the need to make provisions to regulate the operation and future development of the hydrogenated vegetable oil industry so as to maintain, at reasonable prices, supplies essential to the life of community while safeguarding the interests of small investors (Bokhari R., 1989). In the beginning, these new industries were managed by the provincial government. After three years these were transferred to and managed by the Ghee Corporation of Pakistan, a federal government corporation.

NATIONALIZATION OF BANKS

All the commercial Banks were nationalized in January 1974. The Banks Ordinance was enacted which nationalized scheduled local commercial banks and several other smaller banking activities. Some important banks nationalised during 1974 are shown in the following table:

THE MAJOR NATIONALISED BANKS OF PAKISTAN

Table:3.1

1	Habib Bank Limited
2	United Bank Limited
3	Muslim Commercial Bank
4	Commerce Bank
5	Australasia Bank
6	Premier Bank
7	Pakistan Bank
8	Sarhad Bank

Source: Economic Survey 1973–74.

The nationalization of banks was aimed specifically to effect equitable credit

distribution across sectors, regions and income groups to ensure the security and safety of account holders' deposits and generally to direct banking activities towards national socio–economic objectives (Pakistan Economic Survey 1973–74). The reasons for the nationalization of these banks stated by the State Bank of Pakistan was that private banks did not pay adequate attention to their social responsibilities and failed to contribute their due share to the process of broad based growth which would ensure a wider and more equitable dispersal of the benefits of economic development. The banking system had not directed sufficient attention to building up its inherent strength by pursuing appropriate policies in respect of capital and reserves. In the light of the above issues, it was necessary to nationalise them to stop malpractices in the banking system. Nine shipping companies were merged into a Pakistan Shipping Corporation in 1976. The decision of government was based on the hope of better performance by the public corporation as compared to private competitors. The Agro–Industry was nationalized in the last phase of the programme and was perhaps the most controversial event in the whole nationalization. The Ordinance of July 1976, brought control of around 2,000 flour milling, rice milling and cotton ginning units under public control. This nationalization was designed to eliminate hoarding, black marketing, price manipulation and adulteration. The Ministry of Agrarian Management was created to supervise and look after the operation of the nationalized enterprises. These were the measures taken by the government during that period of nationalization (IPS, 1988). However, the government extended the public enterprise sector not only by nationalization but also by an ambitious investment programme, especially in the manufacturing sector.

Mr. Bhutto's government had to face strong opposition from a coalition of political groups. There was a long and furious political movement against government policies which ended Mr. Zalfiqar Ali Bhutto's government as well as its nationalization policy.

DENATIONALIZATION MOVEMENT

In July 1977, following violent political unrest, a Martial Law government took over and started to reverse the policy by a mixture of economic deregulation reforms and selected privatization programmes. The new government of General Zia Ul Haq reviewed the state owned enterprises during 1978 and tried to develop a five year plan.

The Fifth Five Year Plan (1978–83) was developed and major stress was given to the revival of the private sector in Pakistan. An Implementation Committee was established to evaluate the recommendations of the State Enterprise Review Commission. The implementation committee adopted the following measures:

(a) Dissolution of the Board of Industrial Management and the established expert advisory cell (EAC).

(b) Reduction in the number of corporations.

(c) Development of a programme of the financial restructuring of several companies.

(d) Liquidation of chronically sick enterprises.

(e) Denationalization of agro and engineering companies.

The sixth Five Year Plan (1983–88) adopted the government's policy parameters. According to this plan, the framework was based on a new compact between the public and private sectors. The role of these two sectors was explained as follows: 'Policies of coexistence and cooperation will be encouraged in all sectors of the

economy – whether manufacturing industry, agriculture, construction, education, health, services, trade or any other field – and a serious effort made to remove the previous antagonism between these two sectors. The public sector will essentially play the role of a catalyst. It will create the physical and human infrastructure that is needed for private initiative to materialise. It will also reserve the right to enter as an investor of last resort wherever private sector is hesitant to come in because of the large size of an investment, or new technology, or uncertain markets. The directly productive activities and services will be reserved almost exclusively for the private sector both in agriculture and in industry. Private initiative will also be encouraged in providing physical infrastructure in association with the public sector – such as in the construction of highways, airport terminals, energy development and telephone services – as well as in education, health and other social services' (The Plan, p13). The plan envisaged the share of private investment would be raised, from 29% to 44% over the next ten years i.e. 1978 to 1988. For most of the first half of the 1980s the Government of Pakistan's efforts were directed at improving the operational efficiency of public enterprises after the initial denationalization of agro–based units, and it was not until the mid–1980s that privatization reappeared in the government's vocabulary. In May 1985 a Disinvestment Committee was organized to oversee the sale of Rs. Two billion worth of profitable enterprises and to analyze the problems of sick units. The Committee tried to oversee the deregulation and denationalization programmes of Pakistan International Airlines, Pakistan State Oil and Sui Gas etc (Bokhari R.,1989). The main objective was to improve operational efficiency and reduce the financial burden on the government budget. No significant progress was made due to a lack of political will and commitment to implement the whole process. Subsequently, the government established the National Disinvestment Authority (NDA) in 1988 to undertake disinvestment of such units that the government referred to it. The Authority was required to examine the privatization of 14 companies and divestiture of a 20% share of nationalized commercial banks. In 1988 the government

was again changed and the programmes remained unsettled.

PRIVATIZATION POLICY AND THE PPP GOVERNMENT

In December 1988, Pakistan People's Party (PPP), which introduced the nationalization programme during the 1970s, came into power again and decided to carry on the privatization programme. To implement this policy the Government of Pakistan commissioned, in April 1989, N.M. Rothschild and Sons Ltd from UK to prepare and develop a privatization strategy for the Pakistan government and in response to their report, in August 1989, the government established a committee headed by a minister of state for finance in order to oversee the privatization programme. According to the Rothschild Report privatization, through widespread public participation, offered opportunities to make an immediate impact on the government borrowing requirement, increase the ability of the government to fund a social programme, could create incentives and involvement for management and workers, broaden and deepen Pakistan's capital markets, transform the role of the government from proprietor to regulator, and attract foreign investments to fund the expansion.

The report considered a group of enterprises including the Muslim commercial bank, Habib bank, the Pakistan Shipping Corporation, Pakistan International Airlines (PIA), Sui Southern & Northern Gas and Pakistan State Oil. In selling equity in these SOEs the aim was to channel the saving of several hundred thousand private investors into the stock market which currently had an extremely narrow capital base (Slamit Ali, 1989). During the early 1990s the stock market did well but still required a reasonable standard and stability. It was recommended by the Consultant to start with Sui Southern and PIA and in May 1990 the government offered 10% of the share of the PIA valued at Rs. 27.4 million with a guaranteed minimum cash dividend of 12.5% for three years.

The other proposed units remained in the negotiation process and unsold because of the lack of interest in the private sector.

REASONS FOR LACK OF INVESTMENTS

The general public and the investors were not clear about the objectives and commitment of the Peoples Party's government and were aware of the past history and policies of the Pakistan People's Party during the early 1970s. They believed that during the 1970s nationalization, the PPP government placed its own political workers in the nationalised enterprises. As a result of this strategy, the SOEs were characterised by overstaffing, inefficiency, absenteeism, and corruption. Private management of these organisations would not be easy under the circumstances.

The government tried to clarify its manifesto and its objectives and involved foreign consultants to develop the environment of a free economy. But, again the political environment was not in favour of the People's Party government and the government was dissolved by the President of Pakistan and new elections were held under the supervision of a care-taker government. This election brought a new coalition government under the leadership of Mr. Nawaz Sharif.

PRIVATIZATION UNDER THE IJI GOVERNMENT

After 20 months of the Pakistan People's Party government the new government of Islamic Jahmuri Ittehad (IJI) came into power in November 1990. The government had been elected on a manifesto which included vast privatization plans and during the early 1990s it began a vigorous implementation. The IJI privatization policy was one of the most important components of the economic reform programme being implemented in Pakistan. The major objective of this policy was to reduce the drain on government resources caused by the persistent losses of state owned enterprises, and to create greater opportunities for the private sector to expand and modernize

these enterprises with the aim of creating a liberal economic environment suitable for rapid industrialization, in order to accelerate the pace of economic development in the country. The broad objectives of the government were as follows:

OBJECTIVES OF PRIVATIZATION PROGRAMME OF PAKISTAN

Table:3.2

(a) To mobilize resources and reduce the fiscal deficit;
(b) Creating a liberal economic environment in the country;
(c) To improve national profitability;
(d) To facilitate the access of the private sector to financial resources;
(e) Insulating the economy from political interference;
(f) To broaden and deepen the capital market in the country;
(g) Releasing resources for social and physical infrastructure;
(h) To bring employees into share ownership;
(i) To create a more favourable environment for foreign investment.

Source: Privatization Commission of Pakistan– 1993

The IJI government had a specified methodology to achieve the above mentioned goals. Its agenda of privatization covered a wide spectrum of fields: industries, banks and other financial institutions, telecommunications and infra–structure facilities. 10 percent of shares of all such enterprises were ear–marked for sale to employees. In the case of denationalization of previously nationalised units a preemptive right was granted to the previous owners if they were prepared to match the highest bid,

provided the highest bid had not been made by the employees.

The government announced its intention of privatizing almost the entire public sector. Under this open ended policy, the government did not feel obliged to declare the basis of selection of privatization candidates or the sequence of privatization (PC Report, 1992). The government identified 118 SOEs and announced a time schedule to sell them under the specified modes of privatization.

EMPLOYEE PROTECTION MEASURES

Measures were taken to safeguard the genuine rights and interests of employees to minimise their hardships. It was ensured that there would be no lay off during the first year of privatization and the terms and conditions of service of employees would not be altered to their disadvantage. The government intended to undertake labour rehabilitation programmes for surplus workers. A package for such workers were developed along with plans to enable them to take up self-employment on the basis of credit for small scale enterprises and yellow taxi schemes, and training programmes were provided for new jobs and trades. An all Pakistan state owned enterprise workers action committee was established.

Specific parameters which were kept in view while valuing enterprises for privatization. Mostly this process of valuation was done by independent consultants, assessors, surveyors and chartered accountants. Wherever possible the break-up value of the share was indicated on the basis of revalued net assets. If it was not possible to arrive at a break-up value, the value of net assets was established to arrive at a final value of the project. All the valuation reports were reviewed, analyzed and assessed independently by the permanent members of the privatization commission. When they were cleared by the commission, they were placed before the cabinet committee on privatization for consideration and approval.

PRIVATIZATION IN THE FINANCIAL SECTOR

In the Financial Sector, the Muslim Commercial Bank (MCB) and the Allied Bank of Pakistan (ABP) were privatized. The Muslim commercial bank was the first state owned bank to be privatized in Pakistan as a part of the denationalization drive launched by the IJI government. Four bids were received in December 1990 for this bank. The valuation committee, headed by the governor of the State Bank of Pakistan (the central bank of Pakistan) did not recommend the highest and second highest bidders for technical reasons. They invited the third highest bidder, M/S National Group consisting of 12 sponsors with equal shares, to match the highest bid of Rs. 56 per share. This was the major controversial transaction of the IJI government because the committee and the governor of the Central bank did not recommend the higher bidders due to the bidders' past business experience. However, after evaluation of the third bidder's case; the agreement with the National Group was signed on 2nd April 1991, and the management was transferred on 8th April 1991, after they had made the necessary payment of Rs 838.8 million. 25% shares of the Muslim Commercial Bank would be offered to the general public at Rs. 56 per share. Shares in this bank went up to Rs. 110 before falling back.

In the case of the Allied Bank Ltd (ABL), the employees of the bank decided to buy it in May 1991. 7,500 employees gathered Rs.500 million in July 1991 and the Allied bank was divested to the Allied Management Group (see Appendix 3.2). The offer of Allied Management Group to purchase 26% shares of the bank at Rs. 70 per share was accepted by the government and the letter of acceptance was issued on 11th August 1991. The agreement was signed on 9th September and the management was transferred to the employees after the payment of Rs. 495 million and management was required to purchase 25% additional shares within one year at the same price.

The government also wanted "to reduce its dependence on cheap bank credit and to modernize the banking system that has often become hostage to the politics of patronage since Prime Minister Z.A. Bhutto nationalized the country's five major banks in 1974". (Jonathan Friodland, 1991, p44). Since privatization, both privatised banks have improved their performance.

NEW BANKS IN THE PRIVATE SECTOR:

In addition to 8 investment banks, the Government of Pakistan granted permission for 10 new banks in the private sector, and on September 1994 three other private banks were established (The Daily Jang, 19 September, 1994) to strengthen the process of financial reform and promote savings and investment to make the national economy self-reliant.

While announcing the private banking policy Mr. Nawaz Sharif argued that these private banks would discharge their duties and responsibilities in the manner which contributed most effectively to Pakistan's economic transformation into a modern, efficient and self reliant economy. Each of the 10 new banks had to have paid up capital of Rs. 300 million of which 50% was to be put up by the sponsors with an equal amount to be raised through stock market flotation (Muslim Banker 1992). Most of the sponsors of the new banks say they will concentrate on wholesale lending to the corporate customers as well as trade finance. Their greatest immediate concern is to find expert staff to run the banks effectively and efficiently.

The list of private banks with their sponsors and headquarters are as follows:

PRIVATE BANKS OF PAKISTAN & THEIR HEADQUARTERS

Table:3.3

The Private Banks	Sponsors	Headquarters
Bolan Bank Limited	Mr.Javed Yunus	Quetta
First Commercial Bank	Mr. Khalid Ch.	Lahore
Franklin Comm. Bank	Mr. Sohail	Peshawer
First Habib Bank Ltd	Habibs Group	Multan
First Security Bank Ltd	Army Trust	Rawalpandi
First Oversees Bank Ltd	MR.K.Saeed	Islamabad
Mehran Bank Limited,	Dawood & Co	Karachi
Republic Bank Limited	Mr. Zaki Azam	Karachi
Soheri Bank Limited	Feeresta Group	Lahore
Union Bank	Saigols	Faisalabad
Muslim Commercial Bank	Denationalized	Karachi
Allied Bank of Pakistan	Employees	Karachi
Kashmir Bank	Mr. M.R. Khan	-

Source: Interviews, Newspapers and various other sources

It was decided that the headquarters of the private banks will be at all the four provincial capital of Pakistan and Azad Kashmir.

PRIVATIZATION OF INDUSTRIAL UNITS

The IJI government decided in August 1991 to advertise another 100 units in the lot without indicating reserve prices, Some of the terms and conditions of sale were relaxed. Prospective bidders were required to pay in cash 26% of the bid value within one month of acceptance of the bid, 14% at the time of execution of the sale of the agreement, and the balance of 60% in three equal annual instalments or six equal half yearly instalment.

A large number of entrepreneurs showed interest as reflected in the sale of the bid

documents which numbered 745. Actual bids received were 235 for 81 units. Bids were not received for 19 units. The detail of bids document sold and received were as detailed in the following table:

BID DOCUMENTS RECEIVED AND SOLD

Table:3.4

Different Sectors	No of Units	Document Sold	Bids received
- Cement	15	210	55
- Ch.Ceramics	12	114	32
- Roti Plants	16	87	29
- Ghee Mills	22	100	48
- Engineering	6	65	17
- Fertilizer	5	58	9
- Auto Mobile	7	47	22
- Rice Mills	8	35	12
- Misc. units	6	29	11
Total	100	745	235

Source: The Ministry of Finance's Report 1992-93

The bids for 35 units were higher than the reference price or over 90% of the reference price and in the case of Roti Plants more than 80% of the reference price. As far as the remaining units were concerned the highest bidders were asked to match the 90% of the reference price. Some of the units for which offers up to 90% of the reference price were not received and were re-advertised in mid July 1992 in the major national newspaper of Pakistan and the advertisement of was reproduced by the Weekly Wattan London on 25th of July 1992.The following 12 units were re-advertised for sale during 29-30 July 1992 with the new terms and conditions as shown in the following table:

OFFER FOR SALE OF PUBLIC UNITS DURING 29-30 JULY 1992

Table:3.5

Public Units	Earnest Money	Floor Price
Bala Engineering Ltd	2.0 (m)	Rs. 24 (per share)
Bolan Casting Ltd	2.0	Rs. 24 " "
Mustekam Cement	5.0	Rs. 150 " "
A&B Oil Industries	1.0	Rs.90m net assets
Crescent Factory	1.0	Rs. 86.5m " "
Mubarikpur Rice Mills	1.0	Rs.18m net assets
Naya Daur Motors Ltd	5.0	Rs.120 (per share)
Thatta Cement	5.0	Rs. 25 " "
Swat Elutriation Plant	1.0	Rs.25m net assets
Swat Ceramics	1.0	Rs. 10 (per share)
E&M Oil Mills Karachi	1.0	Rs.70m net assets
Dir Forest Industries	1.0	Rs.200m net asset

Source: The Wattan Weekly, London July 25, 1992

The above business enterprises were re-advertised with relaxed terms and with these new terms, the privatization commission received a good positive response from private investors.

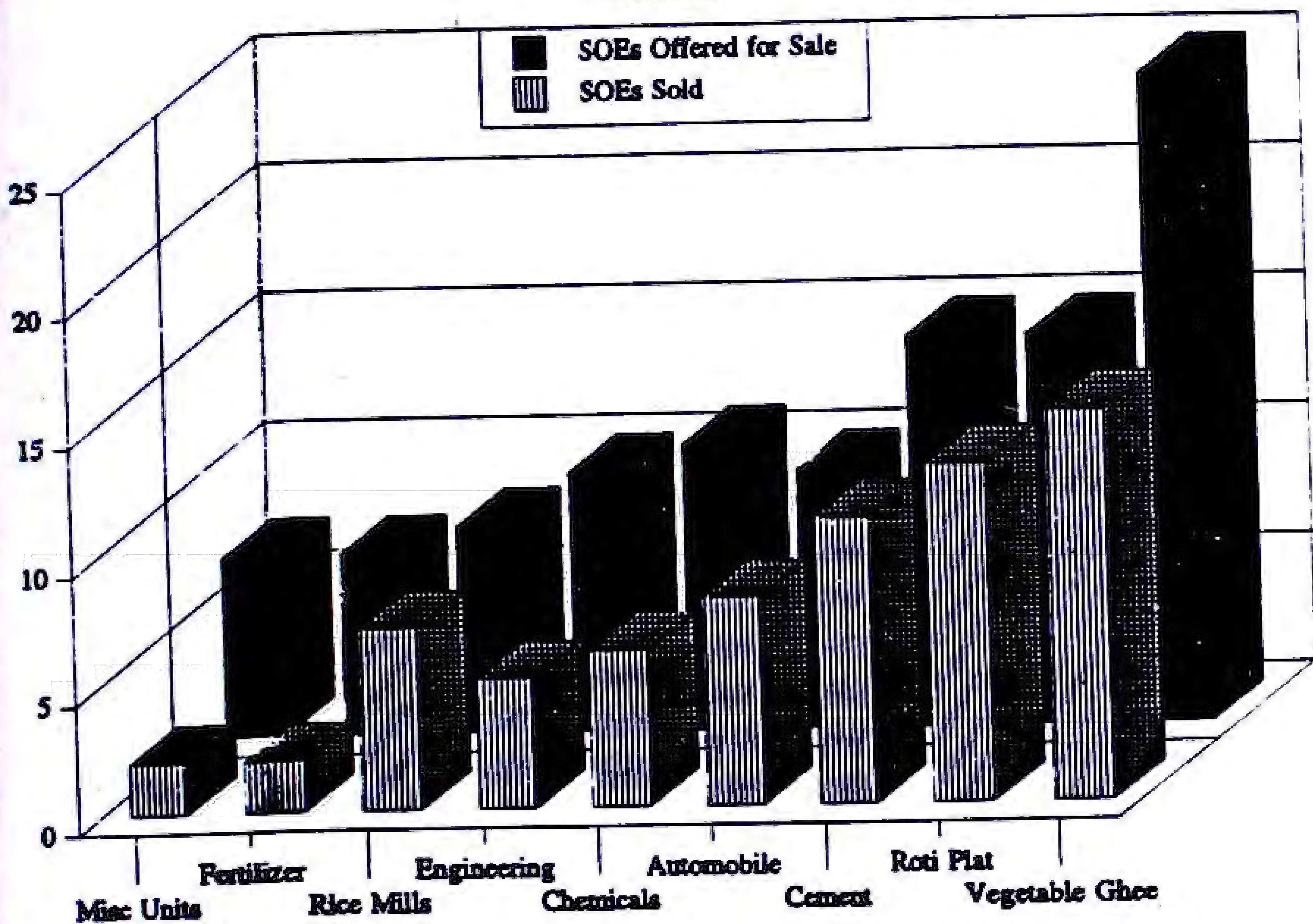
The government undertook a bold and far-reaching programme of economic reforms; trade liberalisation, industrial deregulation, market pricing, the end of exchange controls and more open access for foreign investment. The privatization process and other economic reforms undertaken by the government resulted in a boom in the stock market during the early 1990s and improved the investment climate in the country. The Government of Pakistan announced incentives to foreign investors and provides an infra-structure for setting up new industries in Pakistan.

THE ACHIEVEMENTS TO DATE

The previous government (IJI) privatized 69 public enterprises. The details are shown in the following table:

PRIVATIZATION OF INDUSTRIAL SOEs

Table:3.6



Source: Pakistan Commission Report, 1992–1993

Privatised enterprises which are performing well in terms of profitability and productivity after privatization include: Al-Ghazi Tractor, Pak Suzuki Motor, Pak Cement Ltd, Muslim Commercial Bank, Pak China Fertilizer and Khyber Vegetable Ghee Mills. Other successful examples of enterprises which were sold to the employees include Allied Bank of Pakistan, Dandot Cement, National Cement, Sindh Alkalis, Millit Tractor, Fazalur Rehman Ghee Mills, Pakistan Switchgear, Burma Oil

mills, and Hyderi (Ghee). Overall, it is difficult to assess the impact and performance of all privatised enterprises within such a short period.

The President of the Muslim Commercial Bank, Mr Lawai, said that about 90% of the problems of the banks employees had been solved and exhorted the employees to make the bank the number one bank of Pakistan. He added that 25% shares of the bank were already owned by the people and the time was not far off when 50% of shares would be owned by the general public. The chairman of the bank, Mr Mansha said that no employee would lose his job and no fringe benefits would be withdrawn. Mr. S.M. Munir, Vice-Chairman of the bank, said "the bank has gained people's confidence after privatization because of the professional group who know how to increase the bank's business". According to him the main objective of the Muslim Commercial Bank was to provide better services to the people and not merely to earn a profit. But even then the Muslim Commercial Bank increased Rs. 6 million cash deposits over the first six months after the bank was taken over by the new management (Muslim Banker, 1992). One respondent answered that out of 13,000 employees of the bank in 1,290 branches, 3,500 were found to be employed solely on the basis of political affiliation but he emphasised that those workers would not be sacked. The Muslim Commercial Bank intended to expand its network by opening new branches both inside and outside of the country to accommodate the employees and extend the bank's business.

Allied Bank Ltd is another successful example of an employee buy-out, through employee stock ownership plan. The chairman of the Allied bank, Mr. Latif, said that the deposits of the bank had increased by 200% and about one lac new accounts were opened after privatization(The Bankari, February 1992). The government hope to bring more savings into the banking system to fund expansion and to weaken an

informal finance sector. According to The Pakistan Times September 19, 1992, the first year of the performance of the Allied Bank with reference to various key indicators was as shown below:

FIRST YEAR PERFORMANCE OF ALLIED BANK LTD

Table:3.7

Rs in Million	Aug 90– Aug 91	Aug 91– Aug 92	Rise	%
Pre–tax profits	41	151	110	268
Deposits	21,268	30,950	9,691	46
Advances	10,227	13,447	3,220	31
Import & Exports	16,075	22,564	6,489	40
Foreign Currency Deposits	820	1,515	695	855
Home Remittances	799	1,267	468	59
Industrial Financing	361	2,187	1,826	506
Clientele	1,999,576	2,255,300	255,724	13

Source: Compiled from The Pakistan Time September 19, 1992

The Allied Management Group claimed that these outstanding achievements could be attributed to three factors:

(1) Efforts to provide efficient services and to achieve the confidence of the customers;

(2) The philosophy of employee stock ownership plan (ESOP) has resulted in the greatest possible mobilization of staff as well as giving customers greater confidence in employees;

(3) Better motivation and team work has achieved outstanding productivity.

PRIVATIZATION TREND: TOWARDS PUBLIC UTILITIES

The previous government of the People's Party succeeded in disinvesting a 10% share of the state Airline (PIA). The IJI government's intention was to sell the even bigger four state monopolies, the Pakistan Telecommunication Corporation (PTC), Water and Power (WAPDA), Pakistan Railways and Gas. This new phase of privatization raised different questions about their subsequent regulation, the pre-conditions for sales, how much to sell, how and to whom it should be sold. All these questions and issues are still on the agenda, as the danger is that these public monopolistic utilities could become private monopolies because of their present profit making status. Among these four utilities the Pakistan Telecom corporation (PTC) is considered as the best managed enterprise and is regarded as the jewel in the crown of Pakistan's state industries.

The government has started negotiations with several foreign telecommunications providers including AT&T of USA, Cable and Wireless of Britain, L.M. Ericsson of Sweden and OTC of Australia. The Pakistani government is attempting to encourage outside investment in its expansion programme. Foreign capital is being attracted under the Build Lease and Transfer (BLT) scheme. It expects an eight year pay-back against a 20 year life of the system. Mobile telecommunications are also being offered to the private sector. Paktel of Cable & Wireless and Millicom have set up a system in the market capable of accommodating 35000 subscribers within five years. Also Alcatel, Ericsson and Siemens are expected to install about 500,000 lines under a BLT scheme. The reason for the delay in privatization of Pakistan Telecom was Pakistan Army security, which relies on the utility for its communication but the government has set aside Rs.800 million to enable the Army to set up their own telecommunication network. (Slamit Ali, 1992). A number of

international telecommunications groups could link up with Pakistani partners to bid for the telecommunication system. In the privatization scheme of Pakistan Telecommunications Corporation (PTC), British Telecom, AT&T, Cable & Wireless and Singapore Telecom have shown an interest in investing in this sector.

Pakistan Railways will also be privatized in different phases. Some of the best land owned by the Pakistan Railway has already been sold and some loss making routes have been closed. Passenger ticketing and booking has been transferred to the private sector on six sections of the track. The purchase of the Railways network lock, stock and barrel would be unattractive to even the richest fanatic, so only parts of the operations are going to be privatized. Meanwhile the government of Pakistan has negotiated with French and Swiss Firms to lay a new track and operate high speed trains from Peshawer to Karachi, one of the longest track in Pakistan, in a build own operate basis.

In the Gas industry, on the recommendation of N.M. Rothschild of UK, Rs 2 billion worth of shares of Sui Northern Gas, which has a monopoly in supplying the Gas in the Northern Area, were floated in the stock market in August 1992 but due to lack of public interest the government is considering reducing its share price from Rs 54 per share in order to encourage buyers. Sui Northern Gas is planning to place a total of 34 million shares with British Gas, Sofrage of France and Novacorp of Canada. The shares comprise 40% of the equity of the company.

In the air lines and shipping field, four private Airlines, Aero Asia, Shaheen International, Bowja and Hajweri, are licensed to operate along with 22 privately owned shipping companies. The Pakistan Shipping Corporation is also going to be sold in near future.

In the Water and Power sector, the government organised an international resource group, funded by the US Agency for International Development (USAID), which was asked to develop a privatization plan, in order to ensure the long term goal of bringing electricity to the remaining 60% of the population while introducing private ownership, managerial autonomy and competition through private investors. The plan of the team was approved by the Cabinet Committee on Energy and it was intended to implement the plan in four phases from 1992 to 1996 onwards. The water and power development authority (WAPDA) has a monopolistic position because it generates and distributes electricity across most of the country. Pakistan has about 10,800MW of total installed capacity, 6,557MW is under the WAPDA and the balance under the Karachi Electricity Supply Corporation.

On September 12, 1992, the Prime Minister of Pakistan inaugurated one of the largest private power projects in the world which is known as the 1292MW Hab Project of Pakistan. This $1.7 billion Hab River power project, which was developed as a BOO (built-owed-operate) scheme by Exenel Industries of Saudi Arabia, will boost Pakistan's power generating capacity by about 15% (Frank Gray 1992). This agreement runs for 30 years, and is much longer than the normal BOO contract arrangement of 10-15 years. The Hab River scheme becomes an independent company generating electricity and selling it to the national grid. The managing company being set up to run the scheme is the Hab River Power Group (HabCo). Exenel is the prime sponsor but there are co-sponsors including Mitsui & Co of Japan and British Electricity International of UK. K&M of USA is also the Engineering Consultant and other sub contractors are Campenan Bernard of France, Ansald of Italy and Ishikawajima-Harima Heavy Industries of Japan. There is another 800MW thermal power plant at Jamshoro in Sind province and there is also the power distribution system around the industrial centre of Faisalabad in the province of Punjab. All the above planning and development was done by the IJI

government during its 30 months tenure from late 1990 to mid 1993. The government privatised 69 units and the remaining 50 were in the process of negotiations.

At this time the President of Pakistan utilised his power to dissolve the government on the basis of political unrest and allegations of misuse of government funds. The Supreme Court declared this act illegal but the IJI Prime Minister resigned and chose to have new elections. As a result of this the People's Party came into power in coalition with other smaller parties.

PRIVATIZATION POLICIES OF PPP

The privatization policies of the new government of the Pakistan People's Party do not constitute a new concept or strategy. In December 1988, when the party came into power for the second time, it adopted a new policy of privatization and liberalisation by engaging the British consultant N.M. Rothschild and Sons Ltd which made a comprehensive privatization plan of 14 public industrial units, with a specified period of time for privatization and implementation. This plan failed because of a change of government in 1990. In mid 1993, when the IJI government was dissolved by the President of Pakistan, Mr. Moeen Qureshi, an economist, was selected as a caretaker Prime Minister for three months, and he arranged elections for a new government.

After this election, the Pakistan Peoples Party (PPP) came into power under the Prime Ministership of Ms Benazir Bhutto. This new government again decided to give high priority to a privatization programme as part of a dynamic policy for the rapid socio-economic development of Pakistan.

The Prime Minister of Pakistan reconstituted the Privatization Commission on 25th

November 1993 and, on 8th March 1994, the Cabinet Committee on Privatization, in order to reorganise and accelerate the economic reform programmes. The Privatization Commission decided on three categories of industry, category (A) Small Industrial Units, (B) large-scale manufacturing Units and (C) The Utilities and Services, and a schedule was announced for the privatization of each category:

(A) through open bidding,
(B) though the stock exchanges,
(C) through Strategic Investors.

In the case of large scale service organizations which have a vital role in the public sector, up to 26% will be offered for sale but, for the time being, the state will retain managerial control. In the case of some specified enterprises they will be offered to private investors, whether national or international, along with management control.

According to schedule, the first attempt was made in May 1994 to sell 7 public industrial units but the response was very unfavourable. Another 11 industrial units along with the previous unsold units were placed for sale on 27–31 July 1994. A further 13 small and 21 larger units were scheduled for offer later, while the major public utilities were scheduled to start the privatization process during September–October 1994.

RE-CONSTITUTION OF THE PRIVATIZATION COMMISSION

Initially, Pakistan's privatization commission was established in January 1991 by the IJI government to implement privatization policy in accordance with the terms of reference and policy objectives set by the government. The commission was responsible for the privatization of industrial units, financial institutions and utilities. The government re-constituted the Commission in 1993 and the Cabinet Committee

on Privatization was also re–constituted in 1994 (see Appendix 3.2c).

The newly constituted National Privatization Commission and Cabinet Committee of Privatization decided that privatization programmes and policies should be based on the following main principles:

- privatization will be transparent and equitable.
- no monopoly will be created and procedures should be transparent.
- the banks and utilities will be required to go through a process of pre–qualification.
- financial consultants will be engaged to act as strategic investors and managers.
- privatization should make industries and services more competitive and efficient.
- privatization will be conducted for the benefit of all people not for the few.
- in the power sector, thermal generation will be offered for sale as a whole and hydro generation will remain in the public sector.

The overall objectives of the privatization programme are more or less the same under both governments but there are some differences under the new government, as indicated:

1 To improve the operational efficiency and overall performance of the entities proposed to be privatized and to promote competition.

2 To reduce the financial burden on the government and to release the resources for utilization on the social sector and infrastructure.

3 To promote and strengthen the capital market by increasing the number of share holders.

PROPOSED SCHEDULE FOR PRIVATIZATION

As mentioned above, the National Privatization Commission has proposed the following three categories of industries and services which are identified for privatization along with their time period in the following table:

CATEGORIZATION OF INDUSTRIES AND SERVICES

Table:3.8

Type of Enterprises	Modes of Offer	Time Periods
– Industrial units – Large scale units – Utilities and services	Auction/sale Stock exchange Strategic investor	April 1994 July 1994 Oct. 1994 (was proposed)

Source: Privatization Commission Report 1994

As mention earlier, 118 state owned enterprises were identified by the previous government as candidates for privatisation and 69 of those were sold through competitive bidding until October 1993. The remaining state owned enterprises were to be offered for sale under the following schedule:

- 7 SOEs offered for sale in April 1994
- 11 SOEs offered for sale in July 1994
- 13 SOEs offered for sale later in the year
- 20 larger units placed for sale at the end of the year

Source: Pakistan Privatization Commission, 1994

The first eighteen units offered for sale were as follows:

SOEs OFFERED FOR SALE - APRIL & JULY 1994

Table:3.9

- Hazara Fertilizer
- Swat Elutriationplant
- Sargroh Vegetable Ghee
- E & M Oil Mills
- Marafco industries Ltd.
- PNP Rice Mills Shekupura
- Burma Oil Mills Karachi
- Thatta Cement Co Ltd
- Associated Cement Co Ltd
- General Refectories
- Noshera Chemicals
- Noshera PVC Ltd
- Bela Engineering Ltd
- Republic Motors (pvt)
- Spinning Machinery
- Textile Winding
- Lylpur Ch.& Fertilizer
- Harnai Woollen Mills

Source: Privatization Commission Report 1994.

According to the Daily Jang London August 12, 1994, at the end of the second round of the privatization process, 6 public enterprises from the above list were sold as follows:

PUBLIC ENTERPRISES PRIVATIZED DURING 1994

Table:3.10

-1-	General Refectories Limited
-2-	Harnai Woollen Mill Limited
-3-	Lylpur Chemicals & Fertilizer Ltd
-4-	Republic Motors(pvt) Limited
-5-	Spinning Machinery of Pakistan
-6-.	Hazera Fertilizer (unofficial source).

Source: The Daily Jang London, August 12, 1994

Among the Asian countries, Pakistan is the first country in southern Asia to start an extensive privatization and deregulation programme, despite frequent changes in government in recent years. Privatization in Pakistan is one of the most important economic reform programmes being implemented in the last 15 years under the leadership of the two major political alliances of the Pakistan Muslim League (IJI) and the Pakistan People's Party (PDA), after the period of General Zia's Martial Law. Rolling back the initial privatization programme was not a feasible issue for any government because every party in Pakistan now believed that public enterprises are less efficient than the private sector. The privatised enterprises in Pakistan have subsequently shown an improvement in profitability, productivity and quality of products and services and this improvement has beendescribed to the privatisation of these enterprises.

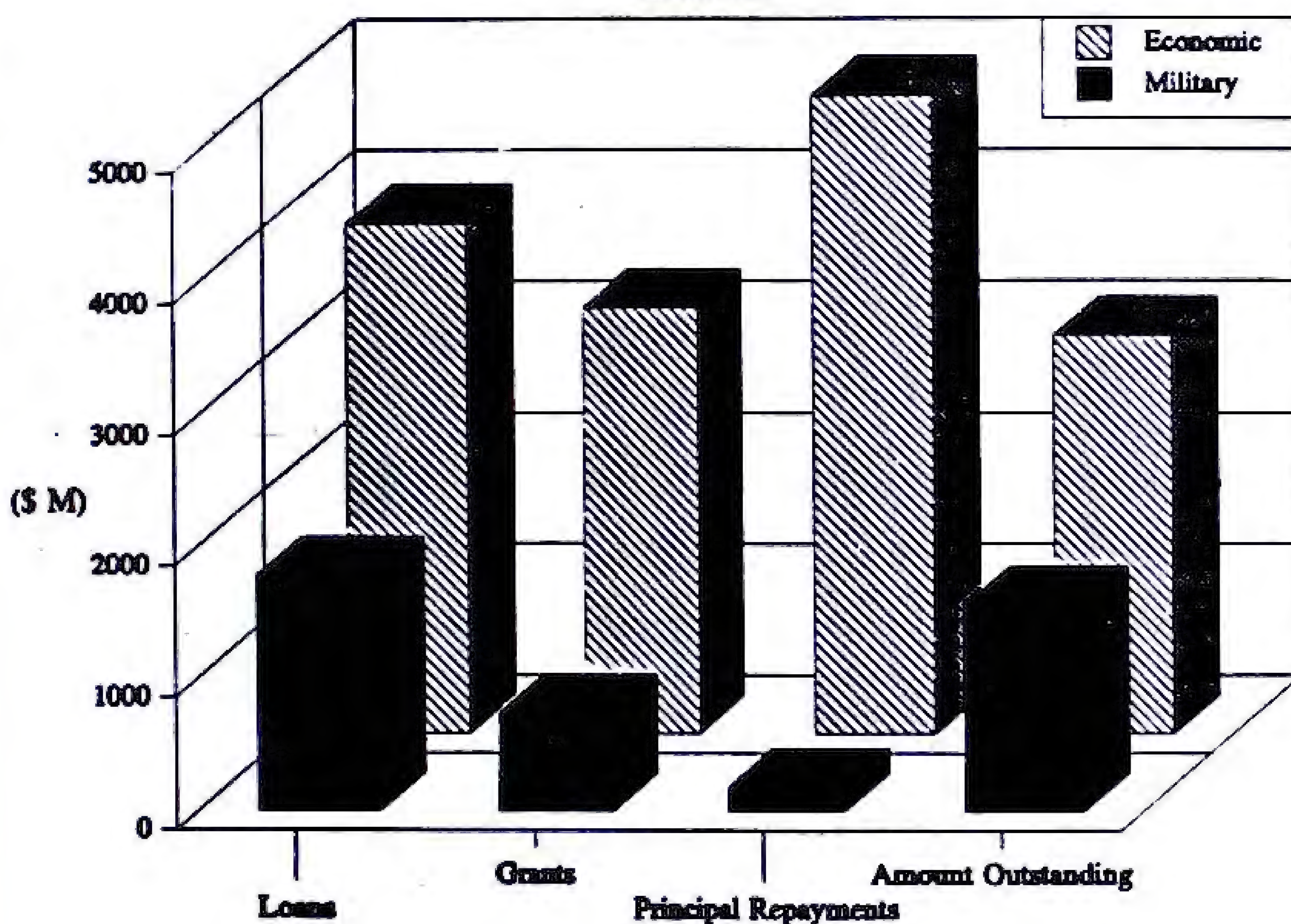
THE ROLE OF INTERNATIONAL AGENCIES

The stopping of American bilateral assistance and the imposition of various restrictions on Pakistan over the last couple of years have threatened economic growth in the country. This termination of the US assistance was a challenge for the Pakistan government as it affected the political and economic situation in Pakistan.

American bilateral assistance to Pakistan, which has been administered through USAID since the 1970s, can be divided into military and non-military sectors for social-economic development. During the 1980s Pakistan was the fourth largest recipient of bilateral US assistance. (Khilji M. K. and Zampelli E., 1991). The following table shows the detailed position of USAID assistance in terms of loans and grants for the last thirty years:

AMERICAN AID ADMINISTERED THROUGH USAID

Table:3.11



Source: Nasir M. Khiliji and Eenest Zampelli, 1991

However, the USA and the World Bank curtailed assistance for Pakistan. The chairman of the Central Board of Revenue noted that the World Bank and the IMF

were in disagreement with the tax system in Pakistan and, in particular, with the tax exemption facilities. They also believed that defence expenditure was excessive and should be reduced. In Pakistan there is great pressure from the general public and the business community on the issue of taxes which has led to strike action and a reluctance to invest. A delegation of IMF provided a framework to improve the tax system and collection procedures.

According to an IMF Survey in 1990 the economy of Pakistan achieved strong growth and moderate inflation during the 1980s. During the late 1980s the government introduced a comprehensive medium–term adjustment and structural reform programme including many policy changes supported by a three year arrangement under the IMF's structural adjustment facility for an amount of SDR 382 million and an 18 month stand–by arrangement for an amount equivalent to SDR 273 million. In addition, the World bank approved US$600 million worth of loans for the agricultural, financial, and energy sector. With the support of these agencies the Government of Pakistan began to tackle many of the country's financial and structural problems. These economic reform measures are expected to correct the financial imbalance and to lay the foundation for a greater involvement of the private sector in the economy, while putting Pakistan on a more balanced and sustainable economic growth path.

In November 1991, the World Bank's Multilateral Investment Guarantee Agency (MIGA) sponsored an investment conference in Pakistan inviting 40 nations of the world. The World Bank also contributed US$300 million to the Hub River power project and other advisoryservices.But during the Ndwaz Sharif government the World Bank was unwilling to get involved until his government began implementing economic liberalization policies. In December 1991, the IMF released 500 million dollars and this added $2 billion in 1991 (Goldestein Carol, 1991). The government

relaxed foreign currency control in February, 1991 and attracted about 800 million dollars due to the attractive interest rate (Pakistan & Gulf Economist September 15, 1990). The public sector grew at an average annual rate of 13.9% during the eighties and domestic debt in the 1990-91 fiscal year reached 422 billion rupees which is about 42.8% of total GDP. Foreign debt grew to more than 15 billion dollars. International aid in the nineties has been affected by the collapse of the Soviet Union and other Eastern European regimes and the perceived need to support reconstruction in these countries.

For this reason among others, the new Government of Pakistan has been trying to develop a good business relationship with USA as a means of furthering its economic development. The US and its advisory agencies were the major influence on the economic reform programme of the budget of 1994-95 (The Muslim, June 1994). Officials of the government of Pakistan have attended international conferences in America and have invited US investors to invest in Pakistan. In the power sector 16 projects worth $4 billion are given, under contracting-out schemes, to US investors in different parts of Pakistan and MIGA is also playing its role in these projects.

Furthermore, World Bank and Asian Development teams have held extensive discussions and meetings with the Privatization Commission and the Cabinet Committee on Privatization to develop a policy framework for the privatization of the telecommunications and electricity industries.

DISCUSSION AND CONCLUSIONS

In Pakistan there has been a tradition of ownership and management of certain strategic areas of the economy by the public sector. These include utilities like Railway, Telephone and Telegraph, Postal services and Irrigation and power. Public

enterprises have their origin either in the days of British control, for example, the Railways and Post Office, were established to develop physical infrastructure and other aspects of transport and communication. Public enterprises were also created to ensure that goods and services essential to the population for social and political reasons were provided at affordable prices. The main objective was to supplement the activities of the private sector efficiently by filling the gap left by private entrepreneurial activities.

It is now thought that efficiency gains are likely to accrue mainly from increasing the level of competitiveness rather than from a change in ownership pattern. In Pakistan, like most developing countries, the process of industrialization was initiated through a strong interventionist policy. The principal element of this policy is a wide range of incentives for introducing industrial investment (Mehsud A. 1990). Private firms have been freed from the requirement of obtaining prior approval for foreign credit against the supply of plant and machinery provided the terms are within the parameters approved by the Government of Pakistan.

There are certain issues in the Pakistan privatization programme, regarding regulatory reforms, privatization modes/strategies, the threat of job losses, and private monopolistic behaviour after the privatization of utilities, which require the establishment of an appropriate regulatory framework before the privatization of enterprises. Perhaps the government should draw lessons from its own past privatization experiences as well as the major international pioneers. It might be useful to recall that one of the important factors which contributed to the large scale nationalization measures of the 1970s was the failure to regulate natural monopolies. It is, therefore, important to establish the legal framework and its operating mechanism before deregulating monopolistic enterprises. Policy makers have to consider how much to privatise, how and to whom these utilities should be sold, and

with what incentives to domestic and overseas investors.

METHODOLOGY ADOPTED IN PRIVATIZATION

The government decided to identified the candidates for privatization through the recommendations of the Disinvestment and Deregulation Committee as approved by the Cabinet Committee. The valuation of these units was carried out by chartered accountants and other specialist independent consultants by a variety of methods such as discounted cash flow, current and future earning capacity, adjusted book value and liquidation value. All SOEs to be sold were advertised in national and international newspapers and sold according to the specified schedule under the specific modes of privatization. The majority of the SOEs privatized through asset sales.

According to the National Privatization Commission, the methodology for the privatization of the different categories of industries and service organizations, sub-categories or specific individual enterprises will vary. The variation is necessitated by the basic differences of scope, structure and organization characteristic of each unit. Another major consideration in adopting a flexible methodology is that, whereas in certain types of enterprises it is in the public interest for all 100 percent shares to be disinvested by the state and offered to the public, in certain other cases the public interest requires that disinvestment take place on a gradual and staggered basis while the state retains management control until such control can be relinquished. Whatever the exact method applied to privatize any unit, large or small, vertical or horizontally, it will be ensured that the process remains fair, open and accountable.

In order to privatize state owned enterprises,the Government of Pakistan has adopted the following methods:

(a) Sales of shares of public enterprises through the stock exchange. This ensured a broad based ownership and the participation of foreign institutional investors.

(b) Sales of individual state owned enterprises were offered by inviting bids from the private sector through a competitive tendering process.

(c) By encouraging the employees to constitute Employees Management Groups (EMG) and by negotiating with them a market price on the basis of an evaluation of assets, liabilities and net worth, along with promoting the concept of an employee stock ownership plan.

(d) By encouraging prospective investment managers to form modaraba (Islamic) companies and raise funds for purchasing shares of state owned enterprises on the basis of a negotiated market price.

(e) Entering into a lease management contract with employees for a specific period to enable them to buy out units ie BLT, BOO and BOT.

(f) By inviting bids from the general public, although efforts were made to encourage employees of the enterprises proposed to be privatized to make bids.

(g) Large industrial units/utilities will be privatize through strategic investors.

All recent governments have recognised the worldwide consensus in favour of an increased role of the private sector in growth, economic development, competition, efficiency and the capital market. Each political group has attached high priority to

the privatization and deregulation process as part of their social and economic development programme for the country. The value of various units sold were Rs. 8.74 billion and receipts Rs. 7.22 billion. Both the IJI and PPP governments have been seriously committed to developing the privatization programme in the last decade. Riyaz Bokhari has said "The government is now clearly committed to an overall policy of gradual privatization of the economy – through deregulation and 'opening up' and selective disinvestment' (1989, p160). The problem is that no Pakistan government has had the opportunity to organized a long–run privatization implementation programme. Furthermore, the role of the international agencies has been more focused on their own interests as well.

The privatization programme and regulatory reforms can be divided into five phases. First, encouraging the private sector up to 1970; second, the nationalization programme of 1971–1977; third, denationalization during 1977–1983; the privatization movement from 1983–1988; and 1988 to date comprehensive privatization programmes. It has, perhaps, been unfortunate that during the past six years, there have been five governments with a variety of policies and priorities regarding the privatization process.

The pioneers of the privatization movement in the developing and developed countries, i.e. United Kingdom, Mexico and Malaysia etc., are fortunate to have had a continuity of governments which helped them to develop long term privatization programmes and implement them accordingly. Pakistan has not had this type of continuity and stability in recent decades. Political unrest is a major disadvantage to the Government of Pakistan and, as a result, investors are reluctant to participate in the privatization programme. However, the social and physical infrastructure as well as the business environment are gradually developing and if any political group succeeds in ruling for a substantial period of time, Pakistan may have the opportunity

to implement a privatization and deregulation policy which will help it gradually to move towards industrialization and self-reliance.

CHAPTER FOUR

PRIVATIZATION IN UNITED KINGDOM: LESSONS FROM EXPERIENCE

INTRODUCTION

A wave of privatization is taking place in almost every region of the world. The United Kingdom was the pioneer in introducing the largest privatization programme of public enterprises and utilities to date. Subsequently, the UK became a leading advisor and exporter of these ideas to the other countries of the world. The idea has been seized on by countries ranging from the super–affluent to the poor, ruled by the governments of the both right and left wings, operating under dictatorships and democracies.

In the UK, major opposition party, the labour party, is also engaged in a wide ranging re–examination of its policies regarding the interrelationship of ownership, control and industrial democracy. As compared to other countries the British privatization programme has been notable in both its scale and its high national and international profile.

This chapter will examine the historical development of the UK privatization programme and will provide details of what has taken place and how it has been organized and implemented. It also examines policies, priorities and problems of implementation and draws lessons from the UK experience for the privatization programme of Pakistan. Before going in to the details of the United Kingdom's privatization programme and experience, it is important to study the historical background of the privatization in UK.

UK POLICIES TOWARDS PRIVATE & PUBLIC SECTOR

Public sector enterprises in the United Kingdom economy evolved from the Nineteenth century onward. In the 19th century municipal level enterprises began to grow including water, gas and other physical infrastructure services. During the early twentieth century the provision of housing also was added role of the local authorities and emerging telecommunications services became a state owned enterprise. During 1939–45, many enterprises came under the control of the Central government (war government) for strategic War purposes.

In the post War period British governments have been formed by either the Conservative party or the Labour party. For most of this period the Labour party has favoured nationalization and public control, where the Conservative party has favoured the denationalization and liberalization. The two parties domination government and conflicting policy stances on nationalization and privatization can be illustrated by the following table summering the policies and programmes of the British governments towards nationalization and denationalization since 1945.

BRITISH GOVERNMENT POLICIES TOWARDS NATIONALIZATION AND DENATIONALIZATION (1945–1994)

Table:4.1

Period	Party In Power	Nationalization And Denationalization Policies
1945–51	Labour	Nationalization of iron and steel industries. Coal mining, electricity, gas, railway, inland waterway, and road haulage industries, Bank of England and Cable & Wireless were all taken into public ownership.
1951–55	Conservative	Denationalization of the iron and steel industries and most road haulage. Sale of council houses under the Housing Act enacted on 1.8.1952.
1955–59	Conservative	Affirmed its belief in the system of free competitive enterprises and its opposition to any further measure of nationalization. Sale of council houses.
1959–64	Conservative	Committed to ensure improved commercial standards of operation and less centralization in those industries already nationalized. Sale of council houses.
1964–66	Labour	Extended public ownership and control over steel and water supply industries.
1966–70	Labour	Set up Industrial Reorganization Corporation. Transferred the private steel monopoly into public ownership and rationalized its structure. Imposed restrictions on sale of council houses.
1970–74	Conservative	Expressed its total opposition to further nationalization of British Industries and committed itself to repeal the Industrial Expansion Act of 1968 which said 'give the government power to use taxpayers' money to buy its way into private industry'. Lifted the Labour's restrictions on sale of council houses.

Period	Party in Power	Nationalization And Denationalization Policies
1974–79	Labour	The aircraft and ship–building industries were taken into public ownership and National Enterprise Board was set up.
1979–83	Conservative	Initiated a radical programme of denationalization and deregulation and services by: (a) Public Offerings 5% of BP(1979) 51.6% of BAe(1981) 100% of AI(1982) 51% of Britoil(1982) 51.5% of ABP(1983) and others (b) Trade Sales BRH (1983) IA of BA (1983) and others (c)Management/Employee Buy–out NFC (1982) and others (d) Sales of Public Housing

Period	Party in Power	Nationalization and Denationalization Policies
1983–87	Conservative	Further privatization measures included: (a) Public Offerings 7% of BP (1983) 22% of C&W (1983) 48.5% of ABP (1984) 99% of Jaguar (1984) 50.2% of BT (1984) 59% of BAe (1985) 48% of Britoil (1985) 31% of C&W (1985) 97% of BG (1987) 100% of BA (1987) (b) Trade Sales BG Wytch Farm (1984) BR Sealink (1984) BA Helicopters (1986) ROr Leads Tank Factory (1986) ROr remainder (1987) NBC (1986–1988) and others (c) Management/Employee Buyout NBC (1986–1988) RG (1987) and others (d) Sales of Public Housing

Period	Party in Power	Nationalization and Denationalization Policies
1987–92	Conservative	Further asset sales by public offering: 100% of RR (1987) 100% of BAA (1987) 36.8% of BP (1987) 10 Water Companies (1989–90) Electricity Companies (1990–91) 2 Electricity Generating Companies (1991–92) BT Shares(1991)
1992–95	Conservative	Further Sale of utilities and enterprises: BT remainder shares (1993) BR franchise offered (1993–94) and Railtrack is on agenda (1995) British Coal (1993–94) Post Office, some Services offered, but overall programme, postponed.

Source: Compiled from various sources.

The above table clearly shows the different policies of the two different parties and their governments.

In every election held since 1945, the two parties have emphasized in their manifestos and policies regarding nationalization and denationalization (see appendix 4.3). Because of these two parties' contradictory policies and their political rivalry, the British iron and steel industry, in particular became a rolling stone between them. Before 1951, the industry which was in the private sector, was first nationalized, and then was denationalized between 1953 and 1963, in stages. The industry was again renationalized in 1967, but in the early 1980's British steel sold a stake to its contracting subsidiaries, Redpath Dorman Long

(Foster C. D., 1992) and then the whole industry was offered for sale in November 1988. It is likely that this type of strategy variation will have an impact on the productivity and efficiency of the industry. However, since 1979, the Conservative party has achieved success in the last four elections consecutively, and has consistently implemented its policies of privatization and deregulation.

It is worth noting the findings of Crewe, that 57% of those asked thought that the privatization of British Gas was a bad idea, while 56% and 72% expressed the same view about the privatization of British Telecom, Electricity and Water respectively (Crewe I, 1988) and more and less same percentage are reported by McCarthy (1990) as well.

According to C.D. Foster (1992) the dominant view within the Conservative party that it was not clear that the privatization would be a vote winner either the electorate or most the Tory back-benchers. Oliver Letwin the adviser of Mrs Thatcher admitted later:

> *"We had no coherent policy. It was not the case that we knew that privatization would bring in millions of new shareholders. It was not the case that we knew all these shareholders would benefit from premiums. It was not the case that we knew companies would do better in the private sector. Almost nothing that has happened since was known in advance. It came upon us gradually and by accident and by leap faith. We had a fundamental distrust in the state running things – that we knew ... It was done in the face of opposition from the industries themselves, from the financial markets and from the civil service. As it slowly turned into a success story, the inertia which had acted against it, started rolling in our favour"* (Foster C.D., 1992, p109).

Other authors such as Young argued that there was a consistent and coherent policy because they mentioned that they would sell back to private ownership

the nationalized enterprises as well as council houses, and strongly opposed the Labour's plan of further nationalization.

They had already seen the pressure of the International Monetary Fund, on the Labour government in 1976, which as a result sold British Petroleum. Young argues that Conservative came to power with a number of specific proposals for deregulation and liberalization. Otherwise, what is the distinctive about the approach adopted towards (privatization) during the 1977–85 period? It has been different from what went before in the sense that it was applied as a philosophy on a sustained and continuing basis (Young S. 1986). This shows that the Conservative party had a well planned proposal of privatization during its second term. But the authors are still in confusion about the domination of political and economic objectives of the Government's privatization programmes and their consistency.

HISTORICAL DEVELOPMENT OF PRIVATIZATION: ROLE OF LABOUR PARTY(1974–79)

While it is true that the general trend of the Labour Party was towards the nationalization especially during its early post war period of the Government when Labour Party nationalised a large majority of the enterprises. According to Whitfield (1993) it is not fair to say that the privatization is the invention of the Conservatives since 1979. There is evidence of deregulation and asset transfer from public to private sector by the Labour Governments. These examples and relevant decisions in different enterprises in different years are as under:

- In 1964, the Labour Government decided to expand the building for the owner occupation, that reflects a long run social advance which pervade

every region and this planned expansion of the public programme was a short term necessity to meat exceptional needs.

- The Labour declared in 1967 that private cleaning contractors could be involved in cleaning the buildings of the government.

- During 1974, the new Labour Government implements main parts of a draft Tory Housing Bill, creating a new third force in the housing, financed by the government, with a large expansion in the role of the housing associations and corporations.

- The Government of Labour also imposed during 1975–77, the major spending cuts, especially in capital spending because of the decline of the public services etc.

- In 1977, £66.8 million BP shares were sold by the Labour Government raising about £548 million net of £22 million expenditure as a part of deal with IMF, 20 per cent of the BP shares were sold to the US by the Labour government, and it was done due to the pressure of International Monitory Fund.

- During 1974–1979 some of the local authorities, Labour controlled as well, as Conservative increased the rate of council house sales without any intervention from the Labour Government. The council house sales exceeded 4% of the stock in the Greater London by 4.5%, South West 4.7%, East Midland 5.9% and South East 7.1%, between 1971–79.

- Proposals were drafted during late 1978 and early 1979 for local

authority DLOs, particularly house repairing and maintenance, to became trading rather than service departments.

Later on, these proposals became the part of the Conservatives' first major legislation for local Government Land and Planning Act 1980 (Dexter Whitfield, 1992). The above historical evidences show that there is a contribution of privatization/deregulation from the Labour Government in process of liberalising the UK economy. Even now, Labour Party has changed its old view of nationalization and is developing a policy not to renationalize the privatised enterprises, including the water privatization which is one of the most controversial.

PRIVATIZATION IMPLEMENTATION SINCE 1979: FOUR PHASE

In the UK privatization started after the success of Conservative party in the election May 1979. The Government under the leadership of Mrs Margaret Thatcher initiated a radical programme of denationalization and privatization of industry and services. The UK government sold its shareholdings in ICL (International Computers limited) and Ferranti, a manufacturer of heavy electrical machinery in 1979, Sinclair and Alfred Herbert in 1980 and 1981 (Foster C.D., 1992 & Yarrow G., 1988). During the same period, a new pattern had been established regarding the conversion of public corporations into the companies, so that they could be then sold. As a result, British Aerospace, Cable and Wireless, Amersham international, National Freight Corporation, British and Associated British Ports were sold (Fraser R., 1988). Whereas, Richardson mentioned that majority of them were not sold as such, during the first Conservative term (1979–83) because of the lack of interest of investors (Richardson J., 1990). The following table shows in details the implementation of privatization programme during the first term (1979–83) of the

Conservative's government:

PRIVATIZATION DURING FIRST TERM (1979–1983)

Table:4.2

Year	Company	Mode	Proceeds
* Nov. 1979	BP	Flotation	290(£M)
Feb. 1981	BAe	Flotation	50
Jun. 1981	BP	-do-	15
Sep. 1983	BP	-do-	566
Dec. 1983	C & W	-do-	275
Jun. 1980	Fairy Engine	Co,Sale	22
Jun. 1980	Ferranti	-do-	54
Feb. 1982	NFC	-do-	7
Mar. 1983	Int. Aerodio	-do-	60
Mar. 1983	BR Hotels	-do-	45
Oct. 1981	C & W	Sh.Offers	224
Feb. 1982	Amersham	-do-	71
Nov. 1982	Britoil	-do-	459
Feb. 1983	Ass.B. Ports	-do-	22

Source: Compiled from Fraser R., 1988 & World Bank Reports

SECOND TERM OF THE UK GOVERNMENT(1983–1987)

The Conservative government took limited privatization initiative during its first term, 1979–83. In its 1983 general election, the Conservatives reinvigorated their privatization policy and included detailed commitments on privatization in the election manifesto. According to the manifesto 1983, Conservative party determined to extend privatization programme to expose state owned enterprises

to real competition, and planned to transfer more state owned businesses to independent ownership. The aim was to sell 51% of the share of the British Telecom to the private sector, and Rolls Royce, British Airways, substantial parts of the British Steel, British Shipbuilders and British Leyland and British's airports would become private sector companies. Substantial private capital would be introduced into the National Bus Company and shares would be offered to those who worked for it.

When the Conservatives came into power again in 1983, the privatization programme grew rapidly in scale. This dramatic acceleration of privatization scale and strategy was due to the keen and continuing interest of the Prime Minister, and the appointment of John Moore as Economic and Finance Secretary to the treasury. He became a determined advocate of privatization in UK and took the view that only well-organized and comprehensive privatization programme could bring political and economic success in the country.

David Marsh (1991) quoted two main reasons for the success of this second stage of privatization: first, the impetus towards privatization came from government, not from the electorate, second, the government adopted the privatization programme for political reasons rather than economic reasons. The main objectives of this phase programme were common with other programmes elsewhere, but the more emphasis was given to the following key objectives of the privatization for this term are as under:

* to increase efficiency through competition, deregulation, or other means;
* to encourage employees to own share in the company in which they work;
* to raise finance which could be used to fund other expenditure priorities,

to reduce borrowing, to reduce taxation, or any combination of these;

- to gain domestic and international prestige,
- to strengthen the capital market.

In terms of the above objectives, the privatization programme has been successful. Millions of the new investors have been introduced to the stock market business with the help of these programme and there was high participation by employees in this privatization programme (Richardson J., 1990). In the early 1984, in the second term of the Mrs Thatcher's government, the pressure increased, with the private sale of Seelink, Inmos and the Wyth Farm, Jaguar and public issues of Enterprise Oil. The government privatization measures implemented during session 1983-87, also included, the disposal of further small tranche of the government's holding in British Petroleum (BP), a further quarter of the equity of the Cable and Wireless, the remainder of Associated British Ports, British Telecom, British Gas, British Airways, a large number of subsidiaries of the national Bus Company and a number of other state owned enterprises as shown below:

PRIVATIZATION PROGRAMME DURING SECOND TERM

Table:4.3

Year	Company	Mode	Proceeds
Sep.1983	BP	Flotation	566(£M)
Dec. 1983	C & W	-do-	275
Apr. 1984	Ass.B Ports	-do-	52
May. 1985	BAe	-do-	363
Aug. 1985	Britoil	-do-	449
Dec. 1985	C & W	-do-	602
Jun. 1984	E. Oil	Sh.Offers	392
Jul. 1984	Jaguar	-do-	294
Nov. 1984	BT	-do-	3,916
Dec. 1986	BG	-do-	5,434
Feb. 1987	BA	-do-	900
May. 1987	RR	-do-	363
Mar. 1984	S Lighgo	Co. Sales	20
May. 1984	Wyth Farm	-do-	80
Jul. 1984	Sealink	-do-	66
Aug. 1984	Inmos	-do-	95
Jun. 1985	Yarrow Ship	-do	34
Nov. 1985	Vosper Thron	-do-	18.5
Jan. 1986	Swan Hunter	-do-	7
Mar. 1986	Vicker Sh.Bg	-do-	60
Jul. 1986	Royal Ord	Inc Sub	201
Aug. 1986	NB.Company	-do-	250
Sep. 1986	BA Helicopter	Sales	13.5
Jan. 1987	Unipart	-do-	30
Jan. 1987	Leyland Bus	-do-	4
May. 1987	DAB	-do-	7

Source: Compiled from World Development(1989)

The above table shows that the British government has adopted three important modes of privatization in order to implement its policies. This term is consideeed quite successful regarding the implementation of the programme, but even the Government could not make some of its agenda during this term.

PRIVATIZATION DEVELOPMENT IN THIRD TERM

During the third Conservative government term (1987–92), a large-scale privatization development programmes were carried out. About 40% of the state owned enterprises had been transferred to the private sector by early 1988. Nearly 650,000 workers became the shareholders of their companies at the time of privatization. 20.5% of the adult population owned shares by early 1988, as compared with only 7% during 1979 (Fraser and Wilson, 1988). The Conservative party in its third term election manifesto announced that it would continue the successful programme of privatization, promising the privatization of the British Airport Authority and the water authorities. The government would also bring forward the proposal for privatizing the electricity industry within the specific regulatory framework.

A White Paper of February 1988, recognized this and recommended introducing several competitors in the generation of power in UK. Nigel Lawson, the Energy Minister, developed an exercise to test how for it would be possible to replace the bulk-supply tariff by which the CEGB (central electricity generating board) sold its electricity to the independent area boards by market base arrangements. So the CEGB was to be divided into two generating companies and a third entity to own and operate the distribution system. One of the generating companies, National Power, was twice in the size of the other so that its fossil-fuel power station base would enable it to carry all the CEGB's nuclear stations into the private sector as well. Each area board was to be privatised

separately, though they would jointly own the grid company.

The water and sewerage industry privatization turned into a complicated process for political reasons, but 10 water companies were sold during 1989-90, further discussion will be in chapter 5. The other third term privatization programmes are stated in the following table:

PRIVATIZATION DURING 3RD TERM OF CONSERVATIVE

Table:4.4

Years	Company	Modes	Proceeds
1987-88	BAA	Sh.offers	1,225(£m)
1988-89	BS	-do-	2.500
1987-88	Istel	Co.Sales	26
1988-89	RG	-do-	125
1987-88	BP	Flotation	5,727
1989-90	10 water	Asset sales	3,480
1990-91	Elect.Cos	-do-	5,200
1991-92	2 Elect.Gen	-do-	2,000

Source: D. Marsh (1991) & Bishop and Kay (1989)

The U.K. privatization programme began during the leadership of Mrs Margaret Thatcher, the "champion" of privatization in the UK politics. She determined to implement her privatization programme in every sector of the business during the decade of the 1980s, which aroused the worldwide interest.

By 1990, at the time of her resignation, around 30 major public sector businesses had been privatized and nearly 800,000 employees were transferred to the

private sector. Initially, Rolls Royce and British Steel remained in trouble after privatization.

FORTH TERM AND POTENTIAL PROGRAMME

After completing the third phase, the Conservative government got a full mandate for the next forth phase. It was the major achievement of Mr Major's Government to win the election for the forth term. Britain had completed a large scale privatization programme during the first three phases and tenure of the Conservative government. This new government also had a privatization agenda before them, including privatization of remaining nationalized industries and the public utilities such as British Coal, British Rail and the Scottish Water. By the Railways Bill 1993, British Railway was split into Railtrack (infrastructure) and passenger services. Two dozen franchises were proposed and they would have rights and duties of operate the passenger service over the infrastructure provided by the public sector Railtrack (Ballingall James, 1993). Now the Railtrack itself is also going to be offered for sale.

The Privatization of British Coal is also on the government agenda, an examination is made of how the announcement of the pit closures in 1992 and subsequent development in the UK coal industry has changed and narrowed the range of available privatization options. There are uncertainties and the problems are likely to arise whichever structure option is chosen for the sale of the British coal, although the most feasible route is appears to be to split the coal industry into two broad regions, with Scotland and other more isolated pits being disposed of separately through auction (Druce and Wright, 1994). Privatization of Post Office was also proposed but postponed (Gattuso Greg, 1994). During 1990s, the Britain privatization programmes will eventually include every sector of economy. By the late 1990s the UK utilities will be competitive even British

Gas will lose its monopoly because the cheaper gas from Siberia will be allowed into its pipelines. The privatization of social services will also be accelerated in domestic as well as international level. By late 1990s both American and British health systems will gravitate towards a system of health maintenance organizations and the local authorities will begin to change their way of providing the municipal services (Macrae Norman, 1992). However, the following table shows the privatization agenda for the 1990s:

PRIVATIZATION AGENDA FOR THE 1990S AND FORTH TERM

Table:6.5

SOEs	Planned privatization and deregulation
B Telecom	Sale of remaining 48.8% stake in 1991–93
BC	The sale of 68 pits and opencast operations planned and some sold 1994
BR	Sales of separate Co.Intercity & franchising and railtrack is on agenda 1995
Post Office	Increased Commercialization & privatization planned but for time being postponed (1994)
NP& Powergen	Sale of remaining 40% stake and NI Electricity
Local Authorities	Sale of 25 airports, 54 ports/harbours, 38 bus co, leisure centres, museums, parks etc
Public housing	To sell–off/transfer remaining 4.5m council homes through state, extension of right to buy/rent
Community care	Residential homes for elderly were sold off
Civil service	Extension of agencies and property service agency and more services contracted out
Motorway & major roads	Privately financed, built and operate roads with tolls to be introduced
Prison services	Private management of new facilities & extended to more of the 120 penal institutions
Trust ports	Sale planned, Dover, Tilbury, Tyne and Aberdeen
Forestay Comm	Owner & Mgt of 2m acres of woodland split 1991
BBC TV/Radio	Royal Charter ends in 1996 and privat. of parts
London Transports	Tendering of London transports and other, bus services

Source: Compiled from D. Whitfield, 1993.

Most of the UK privatization programmes hav been implemented and remaining items are on the current agenda. As Madsen Pirie has acknowledged that *"it is recognised that privatization in Britain is nearing the end of its initial agenda"*, and therefore, there is a scope for directing attention to those services which governments have preferred to keep within the public sector, and to asking if ways can be found to make these services in turn direct their output to the satisfaction of the wants and needs of their customers, that, is to the recipients of the services.

KEY STAGES IN THE UK PRIVATIZATION EPISODES

The UK privatization programme has been implemented through an organised plan and certain stages. John Moore called them three basic parts, such as

> *"Managing the successful transfer of business for public to the private sector in line with objectives that I have described is a lengthy and complex process. It may take two or three years and it can be divided into three basic parts. First, candidate must be identified, the necessary parliamentary authority obtained, regularly structures developed if they are needed, and national objectives secured. Secondly, the companies themselves must be got into a position where they will survive and flourish in the private sector. This may mean injecting new talent, introducing new systems, and reorienting the business to reorganize that its future survival will depend on the service that is given to customers. Thirdly, when market the company is ready, it must be sold to its new owners at price which fairly reflects the exchequer's interest. We do all we can to ensure that the price is the best that can be obtained in the circumstances of each sale"* (John Moore, 1986, p3).

These can be further extended into four key stages of the privatization process regarding the assets sales, which are as under:

TYPICAL STEPS/STAGES TO PRIVATIZATION

Table:4.6

Identify	Public Sector Enterprises Or Corporations
STAGE 1	(a) Feasibility Study (b) Analysis of Options (c) Decision for Options/Modes
STAGE 2	(d) Selecting Advisor (e) Organizational Set-up (f) Regulatory Framework/legal Aspects
STAGE 3	(g) Financial Adjustments (h) Restructuring Enterprises and Corporations
STAGE 4	(i) Selecting Sale Advisors (j) Final Decision and Transfer of Ownership (Sell)

Source: Developed from Moore j.,1986 & Ramanadham V, 1988

(a) Feasibility Study:

When UK government decided to privatize the state owned enterprises and then government identified the right candidates for privatization. After identification of certain candidates, the government hired management consultants and merchant banks to undertake a comprehensive feasibility study and privatization action plan for implementation. This study has to consider all the relevant factors, for example, financial availability, growth potential of national economy, political stability and consistent favourable economic policy of the country, availability of the relevant professionals, level of governmental intervention and profitability.

(b) Analysis of Options:

As mentioned before there are several options and modes available,

According to the economy and political objectives, the government has to decide the right option and mode(s). In case of asset sale which has further choices, such as public offer, trade sales and management or employee buy-outs. Majority of the British enterprises are sold through public offers and also choices were made between a fixed price offer, a tender offer, or a combination of both as these are discussed in chapter eight.

(c) **Selection of Consultants/Advisors:**

In privatization process the role of consultants and advisor, is crucial at each and every stage of the programme. The UK government appointed different advisors and consultants to get more detailed advice on privatization policy and coordination of the asset sales. These consultants played various roles such as general advisers on broader policy matters; consultants to specific areas of government including the Treasury, sponsoring departments and the concerned enterprise; underwriters; stockbrokers; merchant bankers.

(d) **Organizational Restructuring:**

Transfer of ownership from public to private sector requires a preparation and pre-privatization restructuring in order to make the transactions easier. Reorganizational arrangements can be achieved: First, introducing structural changes because it is difficult to transfer the state enterprises to the private sector in their original condition and form. The UK privatization experience shows that public enterprises and corporations required break up and restructuring before privatization eg Britoil, British Telecom and British Rail etc. Secondly, introducing changes in the corporate culture, as most of the UK enterprises

introduced more commercial and business like approach and altered bureaucratic culture by switching management emphasis to neglected areas such as finance, marketing, and human resource management.

(e) Regulatory Framework/legal Aspect:

After finalization of structural adjustments and organizational aspects, a regulatory framework has to be developed regarding price packages, licences and customer care. For monopolistic companies the legislation has to enable the transformation of public enterprises to private limited companies and to define the rights and responsibilities of the private owners. The UK government introduced regulatory frameworks and companies Act legislation before privatization of individual enterprises eg BT, C&W, Gas and Electricity. The regulatory system and legal aspects will be discussed in chapter six.

(f) Financial Aspects:

The adjustment of financial accounts and balance sheets are necessary to ensure that the proposed enterprises are financially prepared for the transition to private sector. This stage of privatization process requires the creation of a commercial track record for the company which would give investors confidence in their investment. This capital structuring also helps reassure the investor that the company has an appropriate financial resources for its future business. Accountant can be hired to prepare a prospectus which contains historical financial and accounting information with all necessary adjustments. At this stage all financial incentives, pension funds, debt write off and other subsidies are discussed and necessary action identified.

(g) **Administrative Arrangements:**

This is a final step in the privatization process, where advisors for sale are selected ie brokers, solicitors, merchant banks and advertisers. The implementation of privatization process and arrangement of these agencies requires effort and coordination within the public administration. UK government has no formal "privatization commission", but a unit in the Treasury for coordination purpose. Each industry and privatization programme is attached to a state minister or secretary of state. The Treasury assumes responsibility for the timing of the sale including the assessment of the enterprises for sale and guides the relevant department in "corporate image advertising" to increase the sale of shares. The UK privatization process shows very extensive and expensive privatization advertising campaigns on all available media to transfer the public sector to private ownership.

The above mentioned are the different important steps and key stages of the successful UK privatization process which is a complicated and lengthy one. The success of privatization programme is not only judged by the process but by the performance, cost and impact of privatization.

THE IMPACT OF PRIVATIZATION

Evaluating the impact of a major policy programme or managerial reform initiative is always problematic. Logically, evaluation would be in relation to whether the stated objectives were accomplished or not, but this assumes:

(a) that explicit and consistent objectives were actively stated; and
(b) the stated objectives were the real objectives being pursued.

Even where the objectives are explicitly and consistently stated, where intended outcome are 'soft' rather than 'hard', e.g. 'culture change' or where a wide range of environmental factors may influence results, it is often extremely difficult to identify and measure the real impacts of particular initiatives precisely. For example, if the preventive objective of health is to improve health by alternative style on the basis of improving understanding created by informing and educating the public, then a very long chain of cause and effect is assumed, and each underlined element of the chain is hard to measure. As importantly, health status has been shown to be influenced by the wide range of social, economic, and culture factors, and therefore identifying the discrete impact of health education is extremely difficult.

Even where the objectives are explicit, and measurement of impacts possible, evaluators are still confronted with decisions about the relevant time scale for impact and evaluation. For example the impact of education investment on economic growth has been shown a long time, 20–30 years, and therefore evaluation after 5 or 10 years would misleading imply policy failure. On the other hand, tax cutting to stimulate retail demand would expected to have rapid, if not immediate, impact and therefore the evaluation point might be 6 months to 1 years. The point to note is that Judgements have to made about relevant timescale and difficult judgements may produce quite different assessment of impact with respect to UK privatization.

Finally, evaluation is inherently about costs and benefits, and therefore unintended, as well as intended, consequences need to be identified and assessed. For example, tax cutting to stimulate retail demand may create and impact boom and balance of payment crisis. The cost would have to be set against the benefits of the policy. Positively, "safe sex" education to control AIDS (Acquired

Immune Deficiency Syndrome) may have benefits effect of reducing the incidence of sexually transmitted diseases. These additional benefits should be set against costs. No area better exemplifies these problems of evaluation than search for enterprise. There are fundamental problems of identifying clear and consistent objectives for the programme. Furthermore, even the inconsistent and often incoherent objectives that can be identified have been argued to disguise much more pragmatic objectives of cost containment and the generation of capital receipts. Measuring impacts such as impact on social and economic efficiency has proven to be difficult, and controlling for exogenous factors, such as inflation or recession at an international level, is equally difficult. Time scale is problematic at the economic and enterprise level, and the potential unintended cost and benefits of privatization are myriad. Each issue is examined below.

Sale of public companies and assets, has been controversial, not least because the government itself took some time to state any objectives at all and then stated an increasing number of apparently contradictory objectives. It was not clear until the speech by the then Financial Secretary to the Treasury, John Moore, in late 1983 that the objectives of the privatisation were stated:

> *"The Government's privatisation strategy is justified on economic and business criteria as well as making in political terms. If the present momentum is maintained, it will help provide a remedy for some of the ills that have beset UK industrial performance in recent years... Managers are set free to mange and new opportunities are opened up ... Pay bargaining can be carried out much more responsibly and easily ... It also enable pride in work and job satisfaction to be increased ... It forces into sharp relief a distinction between activities which are commercial and activities where are not"*

This emphasis on the economic benefits of efficiency had shifted two years later. Speaking in July 1985 about the success of privatisation, John Moore said that apart from achieving greater efficiency, the privatisation policies aimed to

"reduce the role of the public sector and provide substantial sale receipts. They allow employees to take a direct stake in the companies in which they work ... And, importantly, they provide a major stimulus to wider share ownership".

By 1986, the emphasis of privatisation in the UK was being firmly placed on *popular capitalism and wider share ownership*. This was reflected by a further speech by John Moore :

> *"Our programme ... is directed towards the three key areas of life : homes, work-places, and the wider community. We are extending home ownership, increasing employee participation in the ownership of their companies and spreading the ownership of public companies to millions of ordinary people".*

According to Moore, personal ownership *"has an unrivalled power to teach the responsibilities and reward of a free society".*

On the other hand, the official Treasury package on privatisation published in February 1986 elaborated on the aims of privatisation. It states :

> *"The privatisation programme has two main aims : to promote competition and to increase efficiency. These are closely connected. Competition is the best way to ensure that goods and services desired by the customer are provided at the lowest economic cost. Giving customers freedom of choice enables market forces to provide sustained pressures on companies to increase efficiency. Privatised companies generally operate in a competitive market environment. But the government does not wish to confine the benefits of privatisation to business in competitive areas of the economy. Privatisation is therefore being extended to 'natural monopolies' where competition is either unworkable or very limited in scope. To the extent necessary, regulatory arrangement takes the places of the market in holding down prices and ensuring good service for the consumer".*

As can be seen, a number of different and seemingly incompatible objectives are

contained in these statements. Vickers and Yarrow identify seven "significant" aims of privatisation in the UK are as under:

(1) *Reducing government involvement in industry;*
(2) *Improving efficiency in the industries through competition, deregulation or other means;*
(3) *Raising revenue and reducing the Public Sector Borrowing Requirement;*
(4) *Easing problems in public sector pay determination by weakening the public sector unions;*
(5) *Promoting wider share ownership;*
(6) *Encouraging employee share ownership;*
(7) *Gaining political advantage.*

Some of these objectives would clearly require a trade-off against others. For example, if optimising receipts to the Treasury and reducing PSBR were the priority, then privatising public monopolies intact would recommend itself as that would increase their value. This would, however, undermine, if not defeat, the objective of promoting economic efficiency through markets and competition. Equally, if encouraging wider share ownership was the key objective, then discounting against the market value of equity would recommend itself as a mechanism for getting the "small buyer" involved. It would, however, contradict both efficiency and revenue generation objectives.

This situation has produced predictably negative responses from evaluators and academic researchers. Even a sympathetic commentator such as Keljanowski (writing for the Institute of economic affairs!), has noted that the UK privatisation policy is "*... a hard to define mix of objectives, and this implies that none are fully and adequately achieved*". Less sympathetic commentators, such as Kay and Thompson, are much less kind :

> "*The reality behind the apparent multiplicity of objectives is not that the policy has a rather sophisticated rationale, but rather*

> *that it is lacking in any clear analysis of purpose and effects; and hence any objective which seems achievable is seized as justification".*

Mitchell, in a paper provocatively entitled **Privatisation as myth?**, arrives at an even more forceful conclusion. Describing privatisation and the alleged Thatcherite ideology underpinning it, he suggests that it was :

> *"... More an incoherent set of prejudices which borrows aspects of neo-liberalism as it suits, than a principled set of policies. Its primary concern was to perpetuate Conservative rule".*

He suggests further that the multiplicity of stated objectives underpinning privatisation simply disguise "pragmatism and expediency" in coping with Britain's economic decline, bailing out government finances, and satisfying the Conservative's core support.

Whether we agree or not with any or all of the commentators noted, the plurality of objectives stated by government itself, make any simple and clear evaluation of impact difficult. It should be noted that, with the exception of political gain, all the objectives noted fit with the broad objective of social and economic transformation and even a critic as unsympathetic as Mitchell allows that *"The vague faith in markets and desire to roll back the state"* were genuine.

The fundamental difficulty is that ancillary or secondary objectives such as raising revenue and reducing PSBR are more tangible and measurable as policy impacts than the transformational and managerial objectives. This has led Kay and Thompson, Mitchell and other commentators to emphasise the short term financial gains, and to query the reality of other objectives. The plurality of stated objectives and their inconsistency certainly implies the absence of a single coherent integrated strategy, but it does not of course imply that "enterprisation"

was not a core element of the approach adopted.

ASSESSING IMPACTS ON THE UK ECONOMY

This aspect has proven to be most controversial because of the lack of definition of objectives, the wide range of exogenous factors affecting outcomes, the problem of time scale for impact, and the range of intended and unintended costs and benefits that need to be identified and measured.

If we take the broad objective of privatization and reduced public activity creating an enterprise culture and improved economic performance, some potential indicators of impact are listed below :

- Overall public spending as a % of national income did not fall between 1979 and 1992, totalling 42% in each year. The annual average across the period 1980 to 1990 was 41.7% of GDP in comparison with the period of the previous Labour administration (1974–79) when the annual average was 39.6% of GDP.

- Taxation as a % of gross household income remained relatively constant across the period, rising from 37% in 1979 to 39% in 1985 and falling to 38% in 1990. Taxation, direct and indirect, as a % of the average income rose from 36% to 42% across the period due to increase in the scale and scope of VAT (Social Trends 1993). Taxation as a proportion of GDP averaged 41.3% across the period 1980–1990, in contrast to 39% between 1974–1979.

- The PSBR was volatile across the period. In 1979 it was £12.5 billion (at 1992 prices), by 1988–1990 it was negative (the government has a

surplus of revenue in relation to expenditure) before rising to £7.5 billion in 1991, £17 billion in 1992, and a projected £32 billion for fiscal year 1993–94. Proceeds from major equity privatisation were crucial to the achievement of a negative PSBR between 1988–1990 (Economic Trends, 1993.

- Britain's external balance of payments position worsened across the period, from a surplus in 1979 to deficits in all succeeding years, ending with a deficit of £20 billions by 1992 (Economic Trends, 1993, Table 27). International competitiveness measured by relative producer prices and relative unit labour costs worsened between 1979 and 1992 (Economic Trends, 1993, Table 28) despite changes in labour legislation and tax incentives. Annual growth in exports at 3.1% was poor in relation to the EC average of 4.2% and the OECD average of 5%. Annual growth of imports was 4.7% as against the EC average of 4.3% (OECD, Historical Statistics, 1960–1990.

- Economic growth (measured by real GDP and GDP per capita) was around the European average at 2.1% per annum and 1.9% per annum respectively (OECD, Historical Statistics, 1960–1990, Tables 3.1 and 3.2). Interestingly, the data indicates that countries that have not pursued the *"enterprise"* route (eg Norway, Austria, Belgium) and which have substantially higher public spending/GDP ratios, achieve a better growth performance than the UK.

- Trends in employment are also worth noting. The total workforce in employment increased from 25.39 million (1979) to 26 million in 1991. This aggregate comprises substantial growth in private sector

employment (17.9 million to 19.9 million) and a decline in the public sector labour force, substantially due to privatisation transferring employment between sectors (the labour force of nationalised industries/ public corporations fell from 1.85 million in 1979 to 516.000 in 1991) (Economic Trends, 1993, Table 48). Paradoxically, all government employment as a % of total employment was on average higher between 1980 and 1990 at 21.3%, than at any previous time.

- Equally worth noting are trends in unemployment. Unemployment rose sharply 5.6% in 1979 to over 11% between 1982–1986, fell to a low point of 7.1% in 1989, and has subsequently risen to over 10% in 1993. At no point since 1983 has unemployment fallen below two million, and by 1993 it was over 3 million people. While it should be noted that the trend in the UK mirrors international trends, only Spain within Europe and the OECD has exceeded the percentage unemployment rates in the UK.

Even noting their indicative character, none of the data above is supportive of an economic miracle having occurred. Indeed, if we use these indicators for international comparisons, the relative position of the UK has either remained constant or worsened since 1979, in comparison to earlier periods. Two key points should be noted in interpreting the data. First, international trends (eg inflation, recession, etc), have clearly impacted upon the UK in terms of economic performance and levels of spending and taxation. The costs of unemployment, and demographic change, would always have created an upward push on spending. The interesting question is the counterfactual one : If there had not been a government committed to enterprise, what would the trends in

public spending and taxation have been?

Equally, two major recessions at a world level have not helped Britain's economic performance, but it must be noted the underlying problem of weak export performance and high propensity to import goes back to the 1960s at least (Thirwall and Godley). It should also be noted that Britain's relative position has worsened internationally, against countries that, on average, have higher ratios of public spending/GDP than the UK (Mishra, 1991 and Esping-Anderson 1990).

Noting exogenous factors may explain why policy impact has been less than anticipated, but it also raises fundamental questions about the formulation of the policy itself. If the UK is a small to medium sized open economy, poorly insulated from external pressures, was it ever reasonable to envisage that domestic efforts to contain public, and enhance private, activity would have the impact intended? Equally, given governments can directly control only half the agenda – the containment and reduction of public spending, activity and taxation – the other half – the growth of private investment, activity and consumption – was always going to depend on the decentralised decisions of domestic and international economic agents. For both reasons, the impact of the policy was always likely to be unpredictable.

The second point to note is that privatisation has been important practically to the trends noted in the data. For example, receipts from asset sales have been crucial to containing, and for a period eliminating, the deficit in revenues to expenditure, ie the failure of governments to raise sufficient in taxation to cover current commitments. As Whitfield demonstrates, without receipts from sales, at no point would the government have generated a surplus on its accounts and

balanced the budget (Whitfield,1992, tables 6.8 and 6.9). While this resolved the short term financial problems, it has created a longer term "structural gap" at the heart of government finances, as public expectations of service remain disconnected from acceptance of the taxation levels necessary to fund such levels. The burgeoning PSBR's of the 1990s (projected at £50 billion by 1993/94) reflect the longer term problem of running out of assets to sell under the circumstances.

To sum up, the impact of privatization on the economy has had little measurable impact, except on public employment trends. Although direct taxes have been reduced, the demands of government of national and household income have been constant and public spending has grown in real terms. Key indicators of economic performance such as growth, international competitiveness, and balance of payments, suggest no significant transformation of Britain's economic performance. Privatisation proceeds, by permitting the disconnection of expenditure and taxation, have resulted in a structural gap in government finances that could be rectified only by raising taxation, reducing public spending and services, or both.

IMPACT ON COMPANIES:

Performance measurement of companies in private and public ownership is not an easy task. It cannot be considered in isolation from culture, structure, environment and objectives of the organization. Before determining the performance of an organization it is necessary to decide what to measure and how to measure. There are certain problems encountered in the attempt to give operational meaning to the pursuit of better management in government as Metcalfe and Richards (1990) indicate *"The basic dilemma in public management reform is coping with rapidly changing problems while within tight*

resource constraints" (1990, p24). The practical work attempting to improve public or private sector management has concentrated upon the design and application of the more effective concepts and measures of performance and efficiency.

Some economists classify efficiency as (a) price efficiency and (b) X efficiency. The X efficiency is further categories into allocative efficiency and productive (technical) efficiency. According to Parker and Hartley (1991) allocative efficiency is

> *"concerned with socially optimal pricing and investment and more specifically with equating prices and marginal costs, a result which arises in a perfectly competitive economy ... in determining allocative efficiency, competition is the product market is likely to be more relevant than ownership... to study production efficiency, there is still problem of what precisely to measure ... To overcome this, efficiency is considered here using a number of criteria, including financial measures commonly used by accountants in assessing business performance as well as some standard economic measures*" (p193).

Therefore for measurement of performance, the following three indicators can be used:

1 Productivity is measured by both labour and total factor productivity immediately before and after the status change. Labour productivity is easier to calculate but, since it does not allow for changes in inputs other than labour, it can provide misleading picture of an organization's productivity growth. In contrast, total factor productivity relates output changes to change in all input.

2 Employment changes which can be designed to test for a possible 'shake out of labour following a status change, which can help to estimate the

performance under effect of employment/manpower change.

3 Financial ratios are also available indicators to measure the efficiency and profitability of the enterprises (Dunsire, A., Parker D. and Hartley K., 1991). These above are the helpful indicators to give an estimation, in different sector particularly with different objectives of the public and private enterprises, but in real term it is really difficult to measure the real performance. As transfer of ownership is likely to result in pursuit of different objectives, so focusing on measurement of specific objectives, might give a misleading picture of performance and efficiency.

The exercise needs a range of performance measures, including profitability and turnover ratios (i.e. profit before interest and tax (PBIT), profit after interest and tax (PAIT), return on sales (ROS), return on capital employed (ROCE)). Further comparative studies of turnover and physical output along with total factor productivity helps to analyze the performance of the companies. Bishop and Kay analysed performance of public and privatised enterprises by utilising the above measurements. Bishop and Kay further noted that profit have been rising since 1979 in most of the public sector and most rapid growth has been in the BT and British Gas. Due to sectoral growth trend ROCE and ROS have tended to increase since 1979, as shown below, the low margin industries by more than those which were already showing high returns.

PRIVATIZED COMPANIES' MARGINS (ROCE & ROS)

Table:6.7

Privatised Companies	Return on Company (ROC)			Return on Sale (ROS)		
	1979	Priv	1988	1979	Priv	1988
Amersham	n/a	22.5	23.7	16.7	13.6	17.0
ABP	16.1	8.9	14.9	20.4	11.0	20.3
BAA	2.1	6.9	8.6	6.9	20.7	25.0
B Airway	13.7	25.3	15.2	6.7	7.4	9.3
B Gas	20.3	16.9	16.4	14.9	16.4	14.3
BT	4.8	16.7	22.1	10.4	22.3	25.6
Britoil	n/a	55.0	8.7*	41.6	50.7	15.3
C&W	24.1	16.6	28.1	25.1	19.1	38.2
Enter' Oil	n/a	80.6	6.6	n/a	48.6	20.2
Jaguar	–ve	50.3	25.7	–ve	13.7	8.5
N' Freight	11.0	15.7	22.5	2.4	4.6	7.1
R' Royce	–ve	27.0	18.6	–ve	7.8	7.8
Pub.Sector						
B Coal	7.9		4.1	4.6		4.9
B Rail	–ve		5.9	–ve		4.4
B Steel	–ve		13.0	–ve		11.5
E' Supply*	10.0		2.2	12.4		7.2
P Office	7.6		7.6	2.4		4.5

Source: Bishop Matthew and Kay John,1989

The above privatised enterprises are showing increasing ROCE and ROS, but there is a little to suggest that they have increased it relative to the rest of the 1979 public sector, as majority of public sector enterprises are also showing increasing trends.

Bishop and Kay also noted that the nature of productivity gains has varied from industry to industry as shown in the following table:

TOTAL FACTOR PRODUCTIVITY (TFP) IN THE UK UTILITIES

Table:1.8

Utility	Annual Rate of Increase (%)		
	1979–88	1979–83	1983–88
BA	1.6	0.0	2.8
British Coal	2.9	0.6	4.6
British Gas	3.3	–0.2	6.2
British Rail	1.3	–0.4	2.4
British Steel	12.9	8.4	12.4
British Telecom	2.4	2.0	2.5
Electrical Supply	1.4	–1.6	4.0
Post Office	3.7	3.6	3.3
Average	3.7	1.6	4.8

Source: Matthew Bishop and John Kay 1988 and 1989.

Parker and Hartley (1991) also studied UK organizations four years before and after privatization using above measurements, and few showed real performance improvement regarding increase in labour productivity, total factor productivity and labour productivity compared to national trends. Some examples of the results are as below:

EXAMPLES OF PRODUCTIVITY CHANGES

Table:6.9

Organisations	Average Annual Growth in %			
	Labour Productivity		Total Factor Productivity	
	Before	After	Before	After
Royal Mint	–5.5	8.8	–4.5	6.1
Post Office & Telecom	5.0	11.3	2.7	1.5
Rolls Royce	–7.4	12.4	–3.0	3.3
BAe (Nation)	4.8	0.0	0.4	–1.2
BAe (Private)	0.0	7.0	–1.2	2.5
BA	6.2	7.8	5.6	6.5

Source: Hartley et al, 1991.

On the basis of empirical results, on productivity, employment and financial ratios, they concluded that

> *"over the three sets of tests, a substantial number of the organizations studied did not provide completely convincing support to the hypothesis. For policy purposes, our results suggest that simple propositions about organization status and performance need to be qualified and treated with some caution. Changing the status of an organization within the public sector may well not provide the anticipated efficiency gains. Similarly, the source of efficiency gains might lie less in ownership status but elsewhere, possibly in product market competition, and possibly in the quality of management and the incentive they are given in their employment contracts"* (1991, p124).

Therefore this analysis shows that performance, before and after privatization, depend more on quality of management, and related incentives than ownership.

As Yarrow, George (1993) mentioned productivity increase in the nationalized industries as well, see table below:

PRODUCTIVITY INCREASE IN NATIONALISED INDUSTRIES
1960–75
Table:4.10

Organizations	Output per head	Total f productivity
B Airways	150%	145%
B Gas	242%	116%
Electricity	127%	28%
N Coal Board	25%	n/a
Postal Service	-6%	n/a
Telecoms	169%	1255
ALL UK Manufac	51%	28%

Source: Compiled from Yarrow George, 1993

Matthew Bishop and David Thompson (1993), Bishop and Kay (1988) made a comparison of the British utilities before and after privatization. Profitability of the major public and privatized utilities are shown in the following table:

PUBLIC & PRIVATE UTILITIES' PROFITABILITY – PBIT

Table:6.11

Enterprise	Nominal (£m)			Real (1987 prices)		
	1979	Priv	1990	1979	Priv	1990
Privatized						
BAA	11	91	256	20	91	209
B Airway	111	234	433	206	244	353
B Gas	443	1244	1095	823	1244	894
B T	785	1531	3244	1459	1749	2647
C&W	52	56	527	97	79	430
Pub. Sector						
B Coal	137		133	254		109
B Rail	–122		113	–227		110
P Office	34		116	63		95

Source: Bishop and Thompson 1993, and Bishop and Kay 1988

LABOUR PRODUCTIVITY OF THE UK UTILITIES

Table:6.12

Utilities	% of Employment	Range of change p.a. (%)	
		1979–80	1980–90
British Airways	Decreased	7.4	6.0
BAA	Increased	0.6	2.7
British Coal	Decreased	–2.4	8.1
British Gas	"	4.9	4.9
British Rail	"	–2.0	3.2
British Steel	"	–1.7	13.7
British Telecom	"	4.3	7.1
Electricity Supply	"	3.7	2.5
Post Office	"	–0.1	3.4

Source: Compiled from Bishop and Thompson 1993

The above analysis shows that overall profitability, and labour productivity have increased and at the same time employment decreased and unemployment increased. The profitability is not the only criterion to judge performance of the enterprises or utilities. There are various other factors which can be taken into account to measure the performance and productivity of these utilities services i.e. cost, employment, price and quality of products and services.

While discussing the impact of privatization George Yarrow (1993) concluded that

> *"Despite the diversity of economic conditions associated with its constituent asset sales and the limited nature of the evidence that is currently available, it is nevertheless possible to draw some general lessons from British privatization programme ... In particular, the hypothesis that the privatization per se will quickly lead to substantial improvements in the performance of the inefficient state-owned enterprises is not well supported by the data. It is true that, in many cases, there has been a history of improving profitability and labour productivity since privatization, but, over the relevant period, the same is also true of both the private and public sectors more generally ... Many of the industries and enterprises concerned reduced employment considerably during the 1980s, including British Steel, British Coal, British Airways, Associate British Ports and British rail. Although some of the this reduction in employment occurred after divesture, the bulk of it occurred before flotation, and in some cases appears to have been largely unrelated to any immediate plans for asset transfer"* (Yarrow G., 1993, p76-79).

The privatization does not has any great deal of impact on labour wages except increasing the salaries of senior managers and executives of the privatised companies. For example average salaries of executives in privatised companies increased 78%, and annual average non-privatized increased only 14%.

The overall experience shows that most companies have increased their growth

and profits after privatization. In some cases, where the companies were already profits makers i.e. British Telecom and Amersham International etc, its difficult to judge the impact of privatization on their performance. As mentioned earlier, Bishop M., & John Kay, Yarrow George and Dunsire concluded that there are less evidence of improvement after privatization, particularly in measure of technical efficiency as opposed to profitability.

IMPACT ON SHAREHOLDINGS:

Privatization has increased the share ownership because small buyers were given special priority in the allocation of the shares at discounted prices. Employees also have taken the opportunities offered and 99% of eligible workforce of Amersham International and Cable & Wireless bought shares, whereas, BT and BAe's relevant percentages were 96% and 89% respectively (J. Moore, 1992). The UK government offered discounted share to the general public and stake holders of the companies to increase share ownership. As noted before, number of shareholders increased more than 20% since privatization. This percentage would be even higher, but some of the bargainers (often first time share buyers) sold their shares after the first week as they focused on short term profit rather than long term investment. Table shows:

SHARE PRICES AT THE END OF THE FIRST WEEK OF TRADING

Table:6.13

Company	First day of trading	Shares sold (%)	Share price at sale (p)	Increase in share price at end of 1st week	Increase in value of the company (£m)
Amersham	25/2/82	100	142	+35	25
ABP	16/2/83–	51.5	112	+26	6
	19/4/84	48.5	250	+2	1
BAA	28/7/87	100	245(100)	+19	233
BAe	20/2/84–	53	150	+19	28
	14/2/85	47	375(100)	+12*	66
BA	11/2/87	100	125(65)	+68	612
BG	8/12/86	100	135(50)	+29	1576
BP	12/11/79	5	360(150)	+3	9
	26/9/83–	7	435	+3	17
		31.5	330(120)		
BT	3/12/84	50.2	130(50)	+85	3329
BSC	15/12/88	100	125(60)	+5	125
Britoil	23/11/82	51	215(100)	–26	–143
	12/8/85	49	185(100)	+22	99
C&W	6/11/81–	50	168	+18	40
	5/12/83–	22	275(100)	–2	–5
	13/12/85	23	587(300)	+0.5	5
Enterprise Oil	2/7/84	100	185(100)	+1	4
Jaguar	10/8/84	100	165	+7	21
N' Power	12/3/91	60	100(175)	+40	535
Powergen	12/3/91	60	100(175)	+40	328
12.ELC'CO	11/12/90	100	240(100)	+51	2619
R' Royce	20/5/871	100	170(85)	+68	926
Sc' Power		100		+15.5	303
H' Elect		100		+22	202
10 W' COs	12/12/89	100	100(240)	+45	2358
TOTAL	–	–	–	–	13339

* at end of first day.

Notes : The Amersham, BAe, Rolls–Royce, and two of the Cable and Wireless gross proceeds included sale of shares to raise cash for company;

Source: Water Pricehouse 1987& Press reports in the first week of flotation. These figures are reported in press in the week following each sale.

As shown in the above table shares were issued at a discounted rate at the cost of 13.339 billion pounds. Due to people buying share as a bargain and then sell on to the institutions, so ownership diffusion was less than it would have been. The table below shows the diminishing number of shares in privatised enterprises over time and increasing concentration of ownership of these enterprises. The end pattern is not dissimilar to the typical private corporation.

SIZE OF SHARE REGISTER

Table:4.10

Company	Privatisation	Latest Figure
B.T.	3.37 million	2.12 million
British Gas	4.4 million (1986)	2.03 million
British Airways	1.2 million (1987)	250,000
Rolls Royce	1.98 million (1987)	564,000
B.A.A.	2.18 million	561,759
British Steel	650,533	252,000
Water Companies	2.65 million	1 million
English Electricity Cos	8.86 million	2.9 million

Source : HM Treasury, Guide to UK Privatisation, 1994.

% SHAREHOLDINGS OF TOP 10% SHAREHOLDERS

British Gas	76.7
British Telecom	91.2
Cable & Wireless	90.44
Jaguar	91.14
Water	81
Electricity Supply	76

The tables indicate that, despite massive discounting against the market evaluation in the first weeks of trading. The policy of broadening share ownership has been at best only partially effective due to small buyers selling on at a profit. Given the cost of discounting (13,339 million), the cost utility of this strategy is very questionable.

LESSONS TO BE LEARNT FROM UK EXPERIENCE

The analysis of this study shows that UK privatization process is a lengthy and complex one. Although Britain privatization programme has been widely praised and imitated worldwide, but at domestic level, its still not popular among the general public and politicians. There is a substantial criticism from opposition parties regarding huge executives pay rises, excessive price charges for the services and the sacking workers and even cutting their wages. Even past supporters and investors who made billions from this programme began to criticise. Mr Major's government has had to drop some of its privatization plans ie post office.

UK privatization programme is a long incremental development process, with variety of objectives which have differed from time to time and industry to industry. As Bishop and Kay noted

> *"At different time, each of these objectives - revenue, efficiency, finance, wider shareownership - has been sacrificed for others. There has been no consistent rationale for the policy of privatization, rather has appeared to meet particular political needs at particular moments in time"* (1989, p650).

However, this complicated programme and process has significant impacts on economic, companies and community, and provides valuable lessons for Pakistan.

LESSON (1): THE NEED FOR STRATEGIC CLARITY

The first and most important lesson from the UK privatization policy is the need for the strategic clarity. This involves setting and ranking objectives explicitly and then designing privatization strategy accordingly. The UK government never ranked its objectives explicitly, a number were mutually contradictory and none of them were completely fulfilled.

It is clear that aims and objectives were not formulated at the beginning of the privatization programme. The privatization policy was adopted as peripheral but became politically central; a policy that had no clear-cut objectives, but which has become almost an end in itself (Bishop and Kay, 1988). Veljanovski C. (1988) noted that the objectives of privatization evolved with the passage of time, and the emphasis given to particular objectives has been varied in individual case.

This suggests that the government of Pakistan needs to be clear its objectives and priorities at the outset. The relative priority of competition creation, wealth diffusion and income generation should be consciously addressed to avoid the confusion and contradictions of the UK privatization programme. This is the crucial importance in addressing the privatisation of currently monopolistic utilities in Pakistan.

LESSON (2): IMPACT ON THE ECONOMY

As noted above, the economic trends indicate that privatization had little positive impact on the economy. Public spending as percentage of national income did not fall significantly averaging 42% in each year since 1979. Taxation as a proportion of GDP average 41.3% across the period (1980–90), in contrast to 39% during 1974 to 1979. The UK's external balance of payments position

worsened since privatization, where it was surplus and started deficits and ending with a deficit more than £20 billions during 1992. Annual growth in exports at 3.1% was poor in relation to EC average 4.2%. Economic growth, measured by real GDP and GDP per capita was around the European average 2.1% and 1.9% per annum respectively. The Trend the employment increased only from 25.39 million in 1979 to 26 million by 1991. The unemployment is worth noting as it rose from 5.6% in 1979 to 10% in 1993. At no point since 1983 has unemployment fallen below 2 million, and by 1993 it was over 3 million.

This analysis shows a disappointing picture of the UK economy, where policy makers, politicians and managers are highly qualified and well experienced as compared to Pakistan.

Again this indicates that privatization needs to be addressed realistically and seen as only part of an array of policies (fiscal, development, industrial etc) geared toward economic growth and development.

LESSON (3): IMPACT ON COMPANIES

The data on performance (see above tables) shows that most privatised companies are more profitable after privatization, enjoying higher sales/profits and higher share prices. Privatised utilities especially have done well in these terms partly by exploiting their private monopoly power.

However, profit ratios are not measures of either technical efficiency or productivity and are highly influenced by other factors such as monopolistic position and sectoral trends. Total factor productivity (TFP) is a better indicator as it measures technical and productivity directly. The recent report by Centre

for Studies of Regulated Industries (CSRI) shows that total factor productivity of BT growing per year by an average of 7.2% since 1989. British gas has been struggling to increase TFP by a mere 0.4% a year and BAA increased above 1% during 1989–1994. The public sector enterprises such as Post office, British Rail and British Coal up to 1993 have achieved better or equivalent performance.

This result is interesting which shows that the growth and productivity depends on sectoral and industrial trends rather than ownership per se. The privatised companies which grew rapidly after privatization eg Amersham, BT and C&W were growing before privatization as well. Again, this suggests a more complex view of factors influencing company performance of which ownership has nowhere been shown to be the key factor. Most commentators suggests that competition rather than ownership is the key to improving the efficiency of enterprises. There was a little change in the managerial culture in the privatized utilities initially because the competition is very limited and the regulatory agencies lacked co-ordination and power.

This situation has, therefore, had to be revisited repeated and progressively with utility privatization such as BT and BG the deregulation subsequently used to increase competition. Later privatization such as electricity generation and supply, and British Rail have sought to build in serious competition at the outset.

The major lesson for Pakistan is that deregulation, not ownership transfer, is the key to improve performance, and that it is crucial to get it right at the outset rather than having to revisit the industry structure repeatedly after privatization, as this disrupts and may even destabilise the industries concerned.

LESSON (4): PRIVATIZATION AND WEALTH DIFFUSION

The UK government policy was to provide a major stimulus to wider shareownership by allowing and encouraging the general public and employees to take a direct stake in companies. The government emphasis was on popular capitalism and wider share ownership. It involved an invitation to the public and employee to apply for shares at a fixed price, set by government. Other methods, such as tender offers, were regarded as too complex a method of sale to secure the participation of small investors. The government offered discounted shares to encourage the smaller investors but a majority have subsequently sold their shares at a profit and now on average the top 10% of shareholders have around 90% of the equity. The UK government could not achieve its shareownership objectives despite shares being issued at a discounted rate against market valuation at the cost of 13,339 million pound of revenue foregone.

The key lesson for Pakistan, with a much weaker capital market infrastructure and low per capita saving ratio, is that the distributive impacts of privatization are hard to control, and may reinforce existing concentration of wealth. Given ethnic and regional division in Pakistan, this will require very careful consideration.

LESSON (5): IMPORTANCE OF CULTURE AND CONTEXT

The British government proclaimed its privatization programme as a model for other countries but this may not true, especially for Pakistan, where, there are clear differences in the level of infrastructure development, and in the socio–cultural and political system.

UK governments are much more stable generally and one party has held power

for the last 15 years promoting the privatization ideology. In the later stages, where Mr. Major's government is less popular and has a very small majority, it could not fully succeed in implementing its privatization agenda, as the post office case showed.

In contrast, Pakistan's governments are unstable, change rapidly and politically are not in a position to take a strong stance about controversial matters such as privatization. So, there are doubts regarding possibility of speedy privatization of enterprises and utilities in Pakistan. The government needs to develop capital market, improve saving and investment trends along with the infrastructure to make these reform programmes workable.

To sum up, the above analysis of economists and policy analysts, shows that economic case, performance case and shareholdings case in favour of privatization has been unproved in the UK. There is no convincing evidence from the UK experience which show any remarkable performance at an economic, industry and shareholdings level. But it is expected that the privatization will continue across the 1990s with the sale of the remaining enterprises with deregulatory reform programmes rather than repeating regulatory based ownership transfer programmes. Hence, Pakistan has to meet all the preconditions present in the UK ie develop capital market, infrastructure, promote business culture and political stability, and then emphasise competition creation and capital extension rather than ownership transfer. Under these circumstances it is worth considering deregulatory programmes by utilizing methods tailored to the social, political and economic situation of the country.

CHAPTER FIVE

PRIVATIZATION OF UK UTILITIES: LESSONS FROM EXPERIENCE

INTRODUCTION

The British government has developed and implemented a remarkably ambitious privatization programme of public utilities. A utility has been defined as an essential service provided through an infrastructure network, which because it is usually capital intensive and it is highly expensive to develop competing networks, is characterised by an element of "natural" monopoly. These natural monopolistic utilities are included: telecommunication, electricity, gas, water and railways (Rouse Lynda, 1987). The process of transferring public utilities from public to private sector has been completed through denationalization, liberalisation and franchising around the world.

The privatization of the British public utilities has also prompted extensive debate on regulatory frameworks. Initially, in the case of telecommunications and gas, there was no direct provision for the regulation of quality. Subsequently, performance has led both to the introduction of quality regulation for these enterprises and later included the provision for quality of regulation for the privatization of electricity and water.

The new Citizen's Charter announced the government's intention to further to strengthen quality regulation and the first legislation arising from the Charter, the "competition and utility regulation Act" has these objectives as well (Ravizzi L & Thompson D., 1992). Most of the authors agree that privatization works best with competition among alternative service providers and suppliers. Vigorous

competition, may be difficult to achieve in the public utilities for which a small number of private firms exist to bid. The appeal of privatization is strong during the time when hard-passed public officials search for ways to save money and provide goods and services (Morgan D.R., 1992). The privatization of public utilities was started with a view to promote more efficient allocation of resources by encouraging competition, reducing the costs and making the privatized monopoly more responsive to consumers needs and wants. However, there are crucial issues relating to success and attainment of utilities privatization process, regulation, regulatory bodies, which will be consider in this chapter.

The first utility privatization in UK was the floatation of 51% shares of British Telecom in November 1984, raising a total of £3.9 billion, nearly six times larger than any previous business/issue on the UK stock market. The popularity of British Telecom's privatization encouraged a further sale of British public utilities. In December 1986 100% of shares of British Gas (BG) were sold for £5.4 billion. This was followed by British Airways and Airports during 1987. As far as privatization of water is concerned, 10 water companies were sold during 1989-90 for £3.5 billions. Whereas, privatization of Electricity Supply and Generation were sold during 1990-91.

As all these privatized utilities had monopolistic characteristic their privatization required the creation of regulation to control their behaviour in respect of consumer interests. These institutions were the semi-autonomous and industry specific regulatory bodies to oversee the activities of the privatized companies and were known as Oftel, Ofgas, Offer, CAA and Ofwat.

A number of commentators have argued that the need for which documented the such bodies reflects the government's failure to promote more competition and undermine

economic efficiency arguments, especially in the privatization of public utilities and other companies with monopoly or semi monopoly position (Vicker J. and Yarrow G., 1988). This chapter will examine the issues raised above and also consider the effectiveness and weakness of the regulatory bodies.

This chapter will focus on the British utilities, especially British Telecom, in detail in order to assess as a comparative basis strategies for the privatization of Pakistan Telecom. In selling-off most of the British monopolies as a whole, instead of splitting them up, the government ensured their future profitability and underlined its commitment to a politically successful privatization, in terms of wide share ownership and state withdrawal from industrial intervention, rather than the promotion of free competition. That is, the goal of privatization came before that of liberalization.

THE ARGUMENT ABOUT UTILITIES PRIVATIZATION

While the major utilities services in a few countries have been investor-owned especially in the United States, in the majority of the countries these services have been publicly owned. As these utilities have the element of natural monopoly. The strategy of privatization of utilities has therefore raised issues and arguments in developed and developing countries of the world. Lynda Rouse noted two forms of arguments against privatising monopolistic utilities.

The first set of objections which she noted are associated with the importance and quality of services provided by public sector. The argument is that if something is an essential commodity or service, and provision of it is essentially a public service then 'nasty commercialism' has no part to play in it. The second, argument is related to the presence of natural monopoly in these utilities and the need to ensure universal access and protect the public. The argument goes that the commercial companies

can't be trusted with monopoly power, and if these companies are given or allowed it, they will abuse this power to raise prices and make essential services difficult for normal consumers to afford. While discussing public services, Rouse noted: first, there must be universal access to commodity or service in question and therefore the laws of supply and demand have no part to play; second this type of supply should be secure, whereas private sector normally can not ensure the supply services; third, in the case of shareholder owned, the temptation to take short cuts in the interest of profits is just overwhelming. Her theme is that the utility services should be run business like approach while having a state supervision and guidance and in some cases subsidization of the services to the general public. In some cases, government makes the matter worse in the monopolistic utilities because its lack of interest in the share performance which leads to inefficiency. The utility needs well established infrastructure which requires quite lumpy investment and government has also other assignments which causes the standard requirements for provision of services.

The private sector is very commercialized and sets cost–benefits targets and tries to achieve them to satisfying regulator, shareholders and consumers. Moreover, it is easier for regulator to implement regulatory framework for betterment of the consumers in the private sector rather public sector. The government priorities are to raise the short term proceeds by selling monopolistic utilities could not save the consumers from the private monopoly without effective regulatory framework. As Vicker and Yarrow mentioned 'In the long run the British privatization programme will be judged in terms of its effect on economic efficiency. By failing to introduce sufficiently effective frameworks of competition and regulation before privatising such industries as telecommunication and gas, the Government has lost a major opportunity to tackle fundamental problems experienced in the past under public ownership' (1988, p 425). Now the regulatory bodies also realized this problems and they are trying to discourage the monopoly behaviour of the private utilities and

encourage the competition. The UK government received the short term receipts but also paid hundreds of millions fees to the advisors, consultancy and advertising agencies as well.

The National Audit Office estimated that by the time of electricity privatization in 1991 the process would have cost to government £2,375 million, and more than half of which was spent on electricity and water privatization. The cost of privatization of other major utilities are mention as under:

INITIAL COSTS OF UK PUBLIC UTILITIES PRIVATIZATION
Table:5.1

Expenditures in £million	BT 1984	BG 1986	BA 1987	BAA 1987
Direct Costs:				
Underwriting broking etc	74	60	7.8	13.6
Commissions	13	9	2.9	4.2
Banks costs	20	45	7.5	13.2
Marketing	14	40	6.2	10.0
Fees to advisers	6	5	4.3	2.4
Total:	**127**	**159**	**28.7**	**43.4**
Cost of employees' preferential treatment:				
Free & matching shares	51	33	13.1	3.3
Discounted shares	5	4	1.6	
Total:	**55**	**37**	**14.7**	**3.3**
Cost of direct incentives to investors:				
Bonus shares	88	122	13.1	53.9
Bill vouchers	23	63		
Total:	**111**	**185**	**13.1**	**53.9**
Cost of indirect incentives to investors:				
Premium as % of issue price*	91	28	63.0	37.0
Grant total (D&ID)	385	409	120	138

Source: Price Waterhouse, Clarke & Pitellis 1993, p217

* The Premium is computed as a % change in the share price from the paid issue price to the closing price after one week's dealing.

The authors noted that the UK privatization, the shares were undervalued at the launch and when the dealing started, the government recorded losses of billions of pounds, including £1,300 million loss on the day of BT sale of shares and to date costs of UK privatization mentioned in previous chapter 4. This type of practice is not affordable as well as advisable to the government Pakistan at the time of privatization of public utilities. The recent sale of Pakistan Telecom shares was stopped in the September 1994 due to financial irregularities. Therefore, the government of Pakistan should be very careful regarding the future programme of privatization of telecommunication and other utilities.

This chapter will specifically focus on privatization experiences of these utilities one by one in order to draw the lessons for Pakistan privatization programme with special reference to telecommunication sector.

BRITISH TELECOMMUNICATION EXPERIENCE

In the United Kingdom, British Telecom is the major supplier of telecommunication services. BT operates one of the largest network in the world. Its principal business is providing local, national and international services along with a range of other services including fax, telex, radiophone, TV phone, data communication and information services etc. The company aim is to become world's leading and the most dynamic telecommunication company (Hill Roy, 1989). The world's first commercial telecommunication operations began in 1839 with the establishment of a telegraph line between Paddington and West Drayton in London. The telephone was privately developed by Alexander Bell in 1876. Therefore the first telephone exchange was open at 36 Coleman Street in London in 1879. After one year, Edison Telephone Company of London and Telephone Company amalgamated/united to

form the United Telephone Company. Meanwhile, Post Office opened its own exchange to provide telephone services in competition with the private sector and finally 1912 all National Telephone Exchange were taken over by Post Office and overall became the monopoly supplier in the United Kingdom. The government monopoly of General Post Office in telecommunication services continued for some 70 years. In 1980, British Telecom, was split off from the Post Office in an early step as the process of privatization.

The Telecommunication Act 1981 sought to break up BT's monopoly and the opening it up to the competition was the first step to be taken by the government to restructure the telecommunication industry. The Act restructured the British Telecom in three ways. First, the Act allowed the subscribers to purchase terminal from the private sources, who ever they like, provided it meets BT's standards. Secondly, this Act allowed the subscribers to sell off spare capacity on their leased lines. These value added network services (VANS) are a form of direct competition to the data transmission service offered on the public network. Thirdly, the Act made the provision for the licensing of alternative private networks. As a result MCL (Mercury) was licensed to provide services in direct competition to BT. British Telecom has had no choice but to respond on this challenge by attempting to under-cut Mercury tariffs and by reducing its costs. This has been a double attack on the public telephone service by reducing the ability for cross-subsidisation from profitable parts of the industry and by actually reducing the resources available to the domestic service. The process of restructuring and liberalization has finally upset the uneasy balance that existed between business and domestic sectors of the services (Lester H. & Lynk E., 1991). In late 1984 the company privatized and government offered its 51% shares to the public and a regulatory body named as Oftel was established in order to improve the quality of services, price control and efficiency as initial step towards the privatization and deregulation programme.

THE STEP TOWARDS LIBERALIZATION

In 1979, when a new Conservative Government came to power and it had desire to change the BT structure to stimulate competition and develop a free enterprise economy. In September 1979, Sir Keith Joseph Secretary of State for Industry, announced a government review of the GPO's telecommunication monopoly. As a result of the review findings he (Sir Keith) announced in July 1980 that the government intended to restructure the Post Office and relax the monopoly over terminal equipment and value added services.

The Government published a British Telecom Bill in November 1980 seeking authority to divide the GPO into two separate organizations: Post office and Telecommunications. In January 1981, Michael Beesely submitted a commissioned report to the secretary of state for industry regarding the liberalization of the use of British Telecommunications network. This report recommended full freedom for private sector suppliers to use the national network to provide telecommunication services to the third parties at a flat rate. The government introduced a White Paper in July 1982, proposing the sale of 51% British Telecom's shares and creation of regulatory body, the OFTEL. In February 1983, the government accepted the recommendations of Professor Littlechild and announced its intention to abolish BT's monopoly over the telecommunications services.

The Secretary of State was given power to licence competing telecommunications services and to require BT to 'open up' its network by permitting the attachment of the wider range of privately supplied subscriber apparatus. Later, it was announced by government that Mercury was to be the chosen vehicle for network competition. In April 1983, Mercury launched its telecommunications services and it obtained a

25 years renewable licence to operate national and international digital networks in competition with British Telecom. Mercury had been set up by Cable and Wireless, British Petroleum and Barclay Merchant Bank to operate domestic and long-distance communications for business and corporate clients by establishing its own UK optical fibre network.

PRIVATIZATION IMPLEMENTATION PROCESS

First, it was felt that the flotation of BT shares would extend and maintain the momentum of telecommunications liberalization. The government believed that exposure to the scrutiny of the private investors would further stimulate BT to improve its efficiency and that efficiency would be better gained from market forces than from the central government direction.

Second, the important factor favouring privatization was the government's financial position where the major problem faced by the government was to contain public spending as part of the fight against inflation. The borrowing requirement of the nationalised industries threatened public sector borrowing requirement limits. These industries were demanding more money to finance new investment programmes. British Telecom particularly required financial support to speed up its modernization programmes to compete with the Mercury. The government considered privatization as a possible solution which would reduce the demand on state finance and PSBR.

As a result, British Telecom was the first target in the public utilities. It became a PLC on first July 1984, paving a way for the November flotation. On November 1984, 51% of BT's shares were sold to public and a total of 3012 million ordinary share were offered for sale, but it was 3.2 times over subscribed at the offered price of 130p. British Telecom's exclusive privilege to run telecommunication services was removed by the telecommunication Act and was to be replaced by a renewable

licence to operate the network. The licence would require it to maintain a universal telecommunications services throughout the UK, including rural areas, and to continue to provide public call boxes, services for disabled persons and 999 emergency calls.

British Telecom would have to allow other carriers, notably Mercury, to connect to its circuits in exchange for a fee. BT was also required to set up separate accounting and reporting arrangements for equipment-making and marketing and to phase out cross-subsides to these business from public network revenues. National Advisory Committees on telecommunication were appointed in Scotland, Wales, Northern Ireland and of course in England as well. When British Telecom was privatized in 1984, every other industrial country except United States was providing telecommunication services through a state monopoly. Britain had already became clear that technological change was revolutionizing the market for the companies' services and private investors could cope better than the state bureaucrats. Moreover, government wanted to bring in new competitors to diminish BT's monopoly of telecommunication's services. The UK's example has been followed in many other countries of the world. In one way or another Japan, New Zealand, Argentina, Malaysia, Mexico and several other Eastern European countries have privatized their telephone companies.

However, in UK the former public monopoly dominates the industry. In 1995, British Telecom has still 95% of the market in the core business. The pattern of a dominant ex-state monopoly and an official regulator has developed on the basis of the BT experience, and has been repeated with other utilities including Gas, Water and electricity industries.

NEW REGULATION AND COMPETITION

Net work competition is now a main focus of the office of the telecommunication (Oftel). The UK is seeking to facilitate telecommunication development through liberalization and introduction of competition across the board in telecommunications. For example, from "duopoly" position of BT and Mercury has been changes to six competitor/operators and tightening X factor from 6.25 to 7.50 etc to reduce the prices in real terms, increases BT's imperative to improve efficiency.

The UK Cable & Wireless (C&W) was always profitable but it was not a real threat to the BT. After the BT privatization C&W's subsidiary Mercury has been a major competitor of BT in the international operations although it withdrew from domestic services in 1994. Mercury communication handles nearly 19% of the UK's outgoing international calls and claims about 7% of the business market because of its cheaper rate. Oftel has attempted to develop a favourable regulatory system for C&W but at the same time Mercury is still facing high interconnection fees from BT which accuses it of being interested only in high margin business.

The British government is launching radical telecommunication reforms based on licensing dozens of public operators. Some of them are planning to offer long-distance services whereas many more will offer alternative local services by using cable TV network and other modern techniques and this can set up a more liberal and competitive telecommunication industry. The government is also allowing operators of mobile data networks to offer connections between stationary points and to cover long-distance services that compete with BT and Mercury as well. The main operators are: British Rail Telecom Ltd and Sprint international (Stephen S., 1992). The UK has more private telephone networks than any other country in Western

Europe. BT is also trying to be allowed to deliver television programmes over its network while making a logical link between the picture and telephones but it will take a couple of years to be allowed for this operation.

THE PRICE SETTING

Given its initial and continuing monopolistic position the RPI–X formula was adopted for restricting BT's prices. The Price control is not over the individual prices of individual services but over the weighted average of the group of prices called a "basket" and the form of the control is the price cap which is a limit to the annual rate at which the weighted average prices of the basket increase. It is known by a formula (RPI–X) where RPI stands for retail price index, a measure of inflation which is published monthly and (X) is a number proposed by the Oftel for the company. The setting of the price cap begins with an assessment of what is a reasonable rate of return on the capital employed for BT, based on an analysis of its activities and structure and also using the relevant comparisons with other industries. This provides an estimation regarding the possible improvement in efficiency of the company, while combining these estimates with BT's actual current rate of return enables a price cap to be calculated which will bring BT's actual rate of return into with its allowable rate of return at the end of a price control period. This price cap is set for a period of four or five years. The first price cap was set in 1984 at RPI–3 and remained until 1989.

In 1989 the price cap was renewed to RPI–4.5 but within the specified period an other adjustment was made to RPI–6.25. The current price cap is RPI–7.5 and came into force for the four years starting from the August 1993. For services outside the main price cap there has been since 1989 and will continue to be a cap of (RPI–0) on private circuit prices. However, within the main price cap there has been subsidiary cap of RPI+2 on domestic lines rentals. The same price cap was originally applied

to business line rentals and allowed to increase at (RPI+5) since 1990.

A MORI report in 1993 gave the percentages of people who say that the price charged in these utilities is reasonable or unreasonable. The following table shows the percentages and the real position:

PERCENTAGE OF PERCEIVED COST/PRICE OF SERVICES

Table:5.2

Utilities	Elect	Gas	Telecom	Water
very reasonable	4%	12%	3%	6%
fairly reasonable	52	57	34	33
neutral	11	10	9	10
fairly unreasonable	22	12	30	21
very unreasonable	10	5	22	19
don't know	1	3	1	7

Source: MORI 1993

The above data shows that only 37% respondents think price is reasonable and 52% response that price is unreasonable. BT claims that due to a series of price cuts, cheaper weekend rates and other discount schemes, customers are getting high quality and cheaper rates.

ROLE OF OFTEL AND QUALITY OF SERVICE

The Office of Telecommunications was set up at the time of BT's privatization under the Telecommunication Act 1984 as a separate non-ministerial government department acting as a regulatory body. Oftel has a Director General (DG) appointed by the Secretary of State and operates with a high degree of independence. He/she has sole responsibility for the monitoring and enforcement of the licences and he

alone can initiate amendment of licences. The DG has independent advisory, information and investigation functions. He is also responsible for the enforcement of the competition. Oftel's expenditures are provided by the Parliament and generated entirely from the licence fees. In carrying out these functions the Director General is guided by certain defined statutory duties, including the requirement to ensure that the telecommunication services are provided in the UK to meet the reasonable demands for them and that those providing services are able to finance them.

The Oftel has to promote the interest of the consumers, effective competition, efficiency of the service providers and research and development. There are a number of check and balance on the power of the regulator as well, for example the role of Monopolies and Mergers Commission (MMC) in reviewing the proposed licence amendments. Oftel is responsible for maintaining registers for all licences issued under the Act, and approved apparatus and contractors. It also liaises about 170 local Telecommunication Advisory Committees which represent the interests of the consumers in their specified areas. There are four National Advisory Committees of England, Wales, Northern Ireland and Scotland which also provide advice to Oftel's Director General.

Oftel publishes regularly a report on BTs quality of service. A joint British Telecom and Oftel survey report in November 1992, shows that 86% of those asked were either very satisfied (31%) and fairly satisfied (55%) with the British Telecom's service and 53% felt that BT's services represented either very good value for money (8%) or fairly good value for money (45%).

For the installation service, 94% of the residential customers were very or fairly satisfied for the quality of installation service.

The latest data shows that the reliability of network continues to improve, with 99.5% of UK inland call attempts proving successful first time. There are about 122,000 public payphones, compare to 80,000 in 1987 and 96% of them are working order. More than 100 BT shops are open, enabling customers to be shown new products and services.

British Telecom has great potential to improve its services and performances. International comparison indicates that BT has been over staffed and most of these surplus staff are engaged in local network operation, so there is need to restructure the local network operation. BT employed 245,000 people in 1990, reduced to 170,700 in 1993 and now about 150,000 people and this reduction did not effect quality of service. Since privatization, Oftel has estimated that the level of productivity has increased 2–3% per year.

BRITISH GAS EXPERIENCE:

In the case of British Gas Industry, its nationalisation was recommended in December 1945 and implemented through the Gas Act 1948 which was effected from May 1, 1949. Twelve area boards covering all regions were established. The first discoveries of the natural gas in the UK Continental Shelf (UKCS) were made in 1965 and during late the 1970s gas transmission systems were converted into natural gas. The Gas Council and the area boards were converted again into British Gas Corporation (BGC) by the Gas Act 1972, and Further significant discoveries of natural reserves were made by the BGC and its allied companies.

Under the Oil and Gas Enterprises Act 1982 which made provision for the denationalization of the offshore oil assets of the both British Gas Corporation and

British National Oil Corporation (BNOC). This Act 1982, authorized the sale of BNOC's oil and gas production interests and left its trading interest.

According to the above mentioned Act 1982 BNOC was directed to transfer its oil and gas productions to the new company, the Britoil. Therefore Britoil started business as a wholly owned subsidiary of BNOC on August 1, 1982. So, later on this company re-registered as public company on 19 November 1982, when the Secretary of the state offered it for sale up to 255.2 million ordinary shares at the minimum tender price of 215 Pence per share.

The Act 1982, also allowed for the denationalization of BGC's offshore oil assets (Michael Web, 1989). The Government announced on May 7, 1985 that all the assets of the British Gas Corporation would be transferred to the private sector and the shares would be sold to the companies, to the employees of the Gas Industry and the general public as well. Accordingly the Gas Bill was introduced on July 25, 1986 and Office of the British Gas Supply (Ofgas) was also established for development and control of the regulatory systems headed by the Director General Ofgas. British Gas was incorporated on April 1, 1986 as a public limited company acknowledging indebtedness in the principal amount of £2,500 million to be repaid in tranches in each of the next successive years.

According to the prospectus of November 25, 1986, British Gas was offered for sale with shares at a price of 135 Pence, and shares to be sold amounted 4,025.50 million pound. When the offer for sale closed on December 3, 1986, nearly five million people applied to become the British Gas shareholders. This was one of the biggest privatizations of government monopoly. But because of the lack of competition one possibly leading to a private monopolistic utility, this necessitated regulatory price controls in the similar form to that applied to BT. The original BG formula which

operated from 1st April 1987 to 31st March 1992 had the following form:

M = (RPI–2)+Y–K, where:

M = Maximum Average Price = (Non–Gas Cost) + (Gas Cost) – (Correction Factor).

(BG Annual Report, 1992, p9).

On 1st April 1992 a new gas tariff formula came into effect limiting the prices for its 18 million British Gas consumers. The new formula encourages BG to purchase gas more efficiently than the past.

A new tariff formula for gas including an "E" factor as follows:

M = (RPI–5)+(GPI–Z)+E–K,

(Max average price= non gas cost + (gas cost) + (energy efficiency factor) – correction factor).

Therefore the new formula has tightened the restriction on the movement in the non gas element of the price. Introducing the "E" factor, Ofgas objective was to ensure that the formula encouraged BG to consider energy efficiency as well as energy supply as a way of fulfilling consumers needs. The efficiency factor(x) now been increased from minus 2 to minus 5, therefore, British Gas can only raise this part of the price by 5% less than the retail price index. According to Ofgas Director of Competition & Teriff, when Ofgas was created one of its duties was to promote the efficient use of the gas but until the Competition and Services (utilities) Act 1992, it was not given power to complete this duty. So in the light of these Acts the relevant responsibilities of the Director General Ofgas are:

(a) to protect the interest of gas consumers in respect of price charges.

(b) to promote the efficiency and economy on the part of the British Gas.

(c) to promote the efficient use of the gas.

(d) to take care of those who are disabled or elderly persons.

(e) The "E" factor expenditure must be targeted and audited properly.

The MMC proposed a long term formula to end the British Gas monopoly while regulating its cost, competition and benefits for suppliers as well as customers, while allowing gas monopoly until 1998.

BRITISH AIRPORT AUTHORITY:

The Conservative government issued a white paper after considering the growing air transport, on August 2, 1961. The government proposed to establish an authority which could owned the main airports which were controlled by the Ministry of Aviation. Later on June 2, 1965, Airport Authority Act was enacted after having been introduced by Labour government during 1964.

According to the above mentioned Airport Authority Act, the four principal Airports of Heathrow, Gatwick, Stansted and Prestwick were transferred on April 1st, 1966 to the British Airport Authority (BAA). During 1970's the Aberdeen, Edinburgh and Glasgow airports were acquired by BAA from the Civil Airport Authority (CAA). The Secretary of State at the time had announced the new legislation in order to make every major airport a limited company and also to privatise BAA with its seven airport companies. Meanwhile, a regulatory system had also been proposed to control and regulate the traffic distribution and other monopoly aspects of airports.

LEGISLATION PREPARATORY TO PRIVATIZATION

The Secretary of Transport, Nicolas Ridley, announced on 5th of June 1985, that the government had decided to make these airport authorities more efficient and responsive to their clients, and to assist the growth of the Airlines industry.

Therefore, the British government introduced a legislation:

(a) to make every major airport as a limited company under the Companies Acts;

(b) to convert the British Airport Authority (BAA) to a holding company and then to privatize it with 7 airport companies. A system of regulation was proposed to control the monopolistic position of the airport, to regulate traffic and safeguard essential national interests.

The Airport Act enacted on 8th of July 1986 with the following affects

(1) the dissolution of British Airport Authority and vesting of its property, rights and liabilities in the successor company nominated by government as part of initial restructuring and eventual privatization;

(2) the reorganization of other airports undertaking in the public sector;

(3) the overall regulation of the use of airports and imposition of economic control at certain airports.

The government wanted to see the local authorities introduce private capital into these companies. If over 50% of the shares in an airport company were sold by the local authority the company would cease to be in the public sector and would become privately owned. The BAA was reorganised on July 31, 1986 into separate airport companies and on August 1986, it was dissolved and its undertaking was vested in the BAA plc and the shares were owned by the Secretary of state. Separate companies were established for each of the Heathrow, Gatwick and Stansted airports and a group of airports were under Scottish Airports Limited including Aberdeen, Edinburgh, Glasgow and Prestwick. Moreover, British Airport Services Limited was established as the owner of half of the issued share capital of British Airports International which managed the Southend, Southampton and Exeter airports (Fraser and Wilson (1988). During 1987 BAA was reorganized, again, and its sale of the entire issued ordinary share capital was announced on June 15,1987. As a result 260

million shares were offered to the general public and another 240 million were placed for different institutions at the fixed rate of 245 pence.

BAA owns and operates seven UK airports eg Heathrow, Gatwick, Stansted, Glasgow, Edinburgh, Aberdeen and Southampton. It handles about 72% of UK air passengers and some 82% of air cargo, and also manages retail business and acts as consultants around the world.

The year 1993-94 was an excellant year while enjoying the first benefits of UK economy recovery. Despite tight RPI - 8 formula on the South East air port charges, pre tax profits increased by 13% to £322 million. The percentage charges were reduced in the previous year at all the seven airports, Glasgow and Stansted reduced more than 15% during 1994.

The overall highly improving position of the BAA during year ended 31 March 1994 is as under:

Table:5.3

Financial Position (£m)	1994	1993	Change
Revenue	1,098	952	15.3%
Profit before tax	322	285	13.0%
Earning per share	47.0p	41.7p	12.7%
Tangible fixed asset	3,567	3,008	18.6%
Capital expenditure	319	200	59.5%

Source: BAA 1994

Moreover, according to financial year 1994 report, the passengers from £70 million in 1990 to £82 million in 1994; profit before tax increased from £240 million to £322.

BRITISH WATER PRIVATIZATION:

In the case of British Water, another natural monopoly the government's approach shifted dramatically over time. Initially, in January, 1985, government announced that the water authorities were the natural monopolies in most of their functions, and government had to be particularly careful when considering replacing the public monopoly with a private one. Therefore, the government had no intention for privatizing the water industry and no plans to alter the public water authorities. Later however, the government reviewed its policy on water privatization and issued a privatization proposal for the water industry in 1987.

Water privatization was one of the most controversial privatizations of the 1980's. The government undertook the project some what reluctantly, and the first plans had to be withdrawn, but finally the privatization of the water industry was completed successfully in 1989 with all 31 water services companies in England and Wales were privatized. During my study tour to England, Ms Dilys Plant, Head of Information, Ofwat, told that *"Britain is the only country in Europe to have nearly 100% privately owned water supply and sewage treatment system focused on tackling pollution and improving the quality of drinking water"*. The purpose of the office of water services is to protect the interest of the consumers of water and sewage services.

The Director General of Ofwat has power under the water Act 1989 revised by Water Resource and industry Act 1991 along with the Utilities Act 1992, to control and limit the prices which the companies can charge to their customers. The annual increase is restricted to the RPI plus an additional factor "K" which has been allocated to each company for each 10 years from 1990 to 2000 to offset the

significant investment programme to achieve the higher standards and improve efficiency.

Germany has the most expensive drinking water in Europe and Italy the cheapest but Britain was unique in Europe in charging for water and related services on the flat rate basis irrespective of the amount of water used. Now trend is towards the meter systems in some areas of England. Ofwat reviewed price control formula in July 1994 which revised the price limit for the period 1995–2004. Overall the performance of the water and sewage companies has continued to be controversial not only on the matter of charged but also their relationship with their customers.

The Drinking Water Inspectorate in the Department of Environment and the National River Authority (NRA) also have major responsibilities for the qualities of drinking water and the treatment of the sewage and other control of related services. Each company must provide an audited statement to the Director General Ofwat which shows that on average increase in standard charges have not exceed the limit.

The limit is RPI+K+U, where RPI expressed as a percentage increase in the retail price index in the year to the November before the charging year; K is a number set for each company for each year to reflect what it needs to increase the charges by over and above the inflation in order to finance the provision of services to the customers and "U" is the amount of "K" not taken up in previous years. For example if the "K" is 4 and the RPI increase in the 12 months to the previous November is 3% then the average charges increase can be no more than 7%. Therefore "K" is the limit for a "basket of charges",which are the charges for the unmeasured or measured water supply, charges for unmeasured/measured sewerage services, charges for reception, treatment and disposal of trade effluent. Companies performance during 1993 shows that the companies maintained the total level of investment having

passed the peek in expenditure targeted for the last year and the companies have increased their capital expenditure programmes by more than had been expected when their price limit were set. The following table shows the comparative capital expenditure on fixed asset formation:

CAPITAL EXPENDITURE/FIXED ASSET FORMATION

Table:5.8

Fixed asset formation	1991-92(£m)	1992-93(£m)
Water supply	1,332	1,358
Sewerage services	570	455
Treatment & Disposal	986	906
Total	2,888	2,719

Source: Ofwat report,1992-93

As shown in the table additions to the current cost fixed asset in 1992-93 amounted of £2,719 million compared with £2,888 million in 1991-92 (in 1992-93 prices). Water industry investment for the current year accounted for 3% of the Gross Domestic Fixed Capital Formation (fixed asset) are the same as for the previous year in England and Wales.

PRIVATIZATION OF UK ELECTRICITY:

After the First World War the Electricity Industry pursued the economic benefits of scale by building larger power stations and improving the capacity to meet customers' demands. This Process required high voltage transmission lines to carry the output power station throughout the UK. A large regional 132 Kilowatt transmission system was constructed and formed a national grid in the 1930's. During 1950's and 1960's a national transmission system was built and known as the

super grid, operating at 275 Kw and 400 Kw. Because of this the size and efficiency of the power stations rose and their number fell. Due to Central Electricity Generating Board (CEGB) monopoly, there were no power stations built by private sector companies to supply regularly through the super grid, even though legislation was designed to encourage competition.
In spite of, the Energy Act 1983, which introduced the more competition in the Electricity industry, but the industry remained an effective monopoly. The Central Electricity Generating Board (CEGB), was supplier of 95% of the national stations. The CEGB also owned and operated the super grid transmission system industry linkage with Scotland and France and also had a statutory obligation to provide bulk supplies of electricity to 12 area Boards.

All 12 area boards were emerged at the time of privatization into the separate distribution companies and each company owned by its own body of the shareholders in a specific area of electricity supply. The CEGB was mainly divided into two private companies, one the National Power and another the Power Generation; the former owned 70% of the current generating capacity and the later owned 30% including the coal, oil and gas turbine plants (Jeremiah D.L., 1989). There are some liberalization measures which were introduced in the 1983 Act. According to this Act 1983, the area board have had to published several new tariffs which are as under:

(a) the terms on which the board will purchase the electricity generated by the private generators,
(b) the terms on which private generators or suppliers are permitted to use board's supply system for the purpose of providing a supply to any premises,
(c) and the terms on which a board will supply premises supplied by a private generator or supplier including place of private generation.

The denationalization of generating capacity would require the development of the new tariff to define the terms and conditions on which the transmission utility would purchase electricity. The larger the number of parties with which the transmission utility has to negotiate, the more costly and difficult is likely to be the determination of an agreed tariff package for them.

NEW STRUCTURE OF ELECTRICITY INDUSTRY

The UK government's proposal for the privatization of the electricity supply mentioned the government aims which are to develop the advantages of the present structure and to correct its weakness in order to make the industry more effective and efficient. The major steps to be taken to develop the electricity industry were as following:

(1) the CEGB's effective monopoly of electricity generation would be ended.

(2) the National Grid would be maintained and will retain its role in scheduling and directing the use of the power stations.

(3) the obligation of the CEGB to provide bulk supplies of the electricity was ended.

(4) a new regulatory system would be developed to ensure competition and to ensure the prices.

(5) all the 12 area boards would be privatized as a distribution companies and these 12 companies would have to supply in their own areas.

(6) these 12 distribution companies based on the existing Area Boards, would also have the right to generate without creating the monopoly of production and supply.

(7) a substantial new generating companies will be formed from some 30% of the CEGB's existing capacity all of it non nuclear.

(8) the remainder of the CEGB owning remaining power stations including the

nuclear stations.

(9) and the other existing and some potential private generator, who had to contract with the distribution companies and the company or the large customers.

Under this new structure of the electricity industry, the activities of the previous CEGB have been transferred and split into four companies. This was a new strategy of the British government, as in the previous privatization experiences the only target of government was ownership transfer. In later, experience of water and electricity privatization, British government introduce deregulation and encouragement of competition in the industries. The regulators got more independent and commitment on the regulatory framework. According to this new approach and strategy, electricity industry is split into following components/companies:

NEW STRUCTURE OF ELECTRICITY INDUSTRY

Table:5.5

1–	National Power – which owns about 60% of fossil–fired power stations.
2–	PowerGen – this company owns the remaining 40% of the fossil–fired power stations.
3–	Nuclear Electric – which owns and operates the nuclear stations.
4–	The National Gride Company owns and operates the transmission system.

Source: Offer Report– 1993.

The Central Electricity Generating Board (CEGB)'s coal, oil and gas power stations

have been divided between National Power and NationalGen which compete in generation of electricity with each other and with other generators. The former 12 Area Electricity Boards became Regional Electricity Companies (RECs) with shareholding initially owned by the government and later on sold to the public. A new company known as Scottish Nuclear was formed to own and operate by the nuclear power stations in Scotland, and other two Scottish Boards became companies which were also sold to the public.

The transmission and distribution had to be regulated, therefore the Electricity Act 1989 was passed by the Parliament in order to restructure the companies and provide a framework for the regulation. All the necessary provisions under which each company operates are set out in the licences and the regulatory body (Offer) has to enforce them. The National Grid Company is owned through a holding company by the 12 regional companies and operates a high voltage transmission system which remains a monopoly business. So except the Nuclear Companies all electricity companies were now in the private sector. The government remaining 40% shares in the National Power and PowerGen were disposed of in March 1995. A number of other countries especially European repeatedly refer to the British experience and many other developing countries are considering to follow this experience in their electricity industries. The European commission is pursuing the possibilities of competition across its member countries. The US has already established competition in generation and a limited concept of competition in supply as well. New Zealand is also in this process and has separated out the transmission network in order to form a separate business and established charges for use of system for competition purposes in generation and supply. The Chilean government a decade ago adopted this policy of privatising the industry and introducing the competition. The big companies were split into different companies and terms and conditions for them were set for use for transmission and distribution system.

COMPETITION IN ELECTRICITY GENERATION

One of the most important aims of the privatization of electricity industry was to encourage the competition and improve the efficiency, so the Electricity Act 1989 was introduced with some fundamental changes and then introduced competition in the generation and supply of the electricity industry. It is said that competition in generation is a sham because of the domination of the two big companies. Now any company is free to seek a licence to act as a generator and to build and operate power stations under current rules. The office of the regulatory body (Offer) has issued nearly 22 generation licences most of them for gas–fired power stations, since April 1990.

All these are the new competitors in the market to provide the power to the system and to win the market share through the contracts. So these companies have begun to take the market share from the biggest companies. For example, initially National Power and PowerGen accounted for 74% of the electricity sold to the Pool and the other sold 26% only.

Nowadays Nuclear Electric and other generating companies have expanded their share from 26% to 30% and combined shares of the two companies are reduced to 70%. Apart from this, competition in industry comes from other power stations owned by the Industrial Companies who have spare/extra power to sell. These can be Electric de France through the cross channel link and from the Scottish companies because they are nearly doubling in capacity of the interconnector and can sell more to the North of England and Wales. According to the Director General Electricity supply competition is also created by the new independent generating stations.

Five power stations are being built by the National Power and the PowerGen. The Scottish Hydro Electric has increased capacity at Peterhead and Nuclear Electric's Sizewell B is due to be commissioned in near future. Eleven stations are being built by independent power producers together with regional companies. The competition between existing players with their existing capacity, has been enhanced by the significant rate of new entry.

COMPETITION IN SUPPLY SIDE

The unique characteristic of the Britain Electricity supply is that it is one of the very few who participates in a competitive market. There are many examples in the world where competition exist in the generation of electricity only. The UK industry has competition in both generation and supply and a number of participants in each competitive area. Generation and supply must be licensed as separate businesses so if a company is engaged in both then it has to treat each as a separate business. In generation there has been a degree of competition in USA where utilities had started to seek competitive tenders for operation of new stations. It is claimed that UK is pioneered in introducing the thoroughgoing competition in supply. Although a few countries now have elements of this concept for example Norway, New Zealand, Argentina and Chile have competition in electricity supply but the extent of competition is greater in the UK than other countries. In United Kingdom the competition in supply is made possible by requiring the National Grid Company and the Regional Electricity Companies to provide access to any supplier to use the transmission and distribution system with the regulated price.

The competition in supply has been phased over an eight year period. Since April 1990, customers with maximum demand above one megawatt were able to choose their own suppliers. On April 1994 this limit was dropped to customers with maximum demand of 100Kw and by April 1998, all restrictions will be removed and

the whole market will be competitive where no customer will be tied to any local or other supplier.

There is a distinction drawn by the regulatory regime, between RECs operating in their own area, where these companies operate under public electricity supply licence; and companies operating outside their own area where they operate as second suppliers. Generating companies can also be second tier suppliers. Offer has now issued about 22 such licences for England and Wales and 15 for supply in Scotland.

The % of customers who choose and negotiate their own price and supplier has grown since competition was introduced in the electricity supply. Nearly 40% chose to switch their supplier in the first year of the regime and the figure would be around 50% in the next year. This trend has been constant since this policy was introduced.

REGULATION AND QUALITY OF SERVICES

The Director General of Electricity supply is appointed by the minister/secretary of state but acts independently from them. The main duties and responsibilities of the Director General are set out in the electricity Act 1989 and 1992, the important of them are as under:

(a) to secure that all reasonable demands for the electricity are met and satisfied.

(b) to secure that the licence holders are able to finance and carry on the activities which they are authorized by their licences to fulfill.

(c) to promote competition in generation and the supply of electricity.

(d) to protect the interest of the consumers in relation to price and quality of services.

(e) to promote efficiency and economy on the part of licensees and efficient use of electricity supplied to the consumers.

The regulation of electricity generation and supply is significantly different from earlier utility privatization in that it relies on competition to improve efficiency and provide protection for customers. In order to achieve this aim the role of the regulator is to focus on competition policy and its relevant issues.

THE QUALITY OF SERVICES

Until full competition and In order to improve and maintain the quality of services, the Office of Electricity.Regulation (Offer) has set the standard of services for regional electricity companies. Of course, the customers are interested in better quality of services and price control. There is no reason for regulating prices if the quality of services is allowed to deteriorate. The electricity regulator provides guaranteed standards of performance where if the companies fail to deliver the services to a customer at a specified level then the customer will receive a compensation payment from the company, which recently increased to £20 per incident. Secondly, the overall standards of performance requires companies to maintain particular services at a specified level for a given percentage of overall cases. The office of the regulatory body publishes statistics showing the comparative performance of the companies against each standard set by Offer. There is much interest among companies, customers and their representatives in the relative performance of each company against the standards. In general, statistics show that overall performance is above international norms but there are complaints that some companies are providing the lower quality of service than others. According to the Director General *"there is every reason to believe that the standards have been maintained and in many cases improved since privatization. In some cases companies have volunteered to meet higher standards than prescribed because of the competitive trends"*.

Apart from Offer, there are consumers' committees in each region and their role is

to provide advise to DG on the guaranteed standards of performance to be observed by them regarding the companies. The office is also responsible for the quality of meters manufacturing and settling the consumers' complaints. In this way, together Offer and committees provide all necessary protection to the consumers including domestic, commercial and industrial.

According to a report of 1993, produced by the MORI, the service provided by the electricity companies leaves 45% of the people totally or very satisfied compared with 54% of the Gas users who say the same about gas services and nearly 6% of the people are dissatisfied with the electricity's services. A majority of people around 79% feel that privatization has had no effect on services they received from their electricity companies.

The following table shows consumers satisfaction with services they receive from each of the utilities discussed above:

THE SATISFACTION % OF UTILITIES SERVICES

Table:5.6

	Elect.	Gas	Telecom	Water
totally satisfied	9	12	9	8
very satisfied	36	42	32	27
fairly satisfied	40	35	44	35
neutral	7	5	7	11
fairly dissatisfy	4	3	5	7
very dissatisfied	1	*	1	1

Source: Compiled from MORI based data, 1993

Overall 64% the electricity supply is seen as reliable with two-third of the people saying they are very or totally satisfied if the natural and fairly satisfies are taken into consideration then the percentage rise substantially to 94% and only 4% consumers are totally or very dissatisfied with the electricity's services.

According to the MORI research data on consumer perception of performance, there is a little difference between pre and post privatization performance. The following table shows the post performance of the UK's four important utilities:

THE % OF PUBLIC ATTITUDES FOR PRIVATIZED UTILITIES

Table:5.7

Changes since privat.	ELECT	GAS*	BT*	WATER**
Improved a great deal	1	2	3	*
Improved a little	6	11	14	3
Stayed the same	79	74	64	70
Get a little worse	5	4	10	12
Got a lot worse	3	2	5	7
Don't know	6	6	4	7

Source: MORI 1993,* Excluding non-user** England & Wales

The above table is showing the attitudes of consumers regarding services of the utilities, how they improved or got worse their performance after the privatization. British Telecom and the Water companies evoke the strongest response in the survey as 19% feel that Water services have got worse and only 3% feel that they improved since privatization. As far as British Telecom's services are concerned only 17% people feel that BT's services have improved and 15% feel that these have deteriorated since privatization.

LESSONS FROM UK UTILITIES PRIVATIZATION

(a) CONTEXTUAL LESSONS:

Historically the UK utility sector has been developed with a well established social and physical infrastructure. All the necessary networks, infrastructure and commercial environment and culture were developed before the privatization. Furthermore, a series of direct meetings, regular briefings and promotional campaigns were introduced to create a privatization environment and attract potential shareholders and investors. However, the 1980s was the experimental and transitional phase for the British utilities. As noted in chapter 4, the monopolistic power of privatised utilities were progressively deregulated and liberalised, and as a result, customers can be protected from monopolistic behaviour. As discussed earlier, the majority of the customers feel that privatization of public utilities has no effect on the quality of services.

Again, Pakistan government initially needs to rank its objectives and priorities before privatization of utility services. Creation of a privatization environment such as promoting high saving trends, developing infrastructure, encouraging competition, developing financial institutions and political stabilization are the prerequisites for privatization policy.

(b) COST OF PRIVATIZATION

Privatization of public utilities costs substantial amounts of money in the different stages of the privatization process, eg feasibility studies and restructuring of legal and financial aspects. Further cost is involved in educating the people, marketing shares in companies, consultants fees, transportation, office management, etc.

The cost of the privatization of 10 water companies in England and Wales included nearly £22 million on advertising alone. British telecom, electricity, BAA, British

Rail and British Gas privatisation have required campaigns on the mass media to achieve mass participation.

As discussed in chapter 4, substantial costs in discounted and free shares, sales forces, restructuring and reorganising were involved. The government spent more then £2,816 million during the last decade to transfer public sector companies to the private sector. The government hired dozens of financial advisors, solicitors/ lawyers, accountants and auditors for the privatization of utilities and paid them millions of fees. The following table shows the summary of costs of major asset sale:

COSTS OF MAJOR ASSET SALES AS % OF PROCEED

Table:5.2

Companies	Expenses (£m)	% Of Proceeds
Cable and Wireless	7.00	3.10
British Aerospace	6.00	3.80
Amersham International	3.00	4.60
Britoil	17.00	3.20
Associated British Ports	2.00	11.20
Enterprise Oil	11.00	2.80
British Telecom	263.00	6.80
British Gas	360.00	6.40
British Airways	42.00	4.70

Source: Compiled from George Yarrow 1993

As can be seen, the UK government spent between £2 million to £360 million on the privatization ofthe enterprises and utilities. The highest expenditures of £360 were incurred on the privatization of British Gas and lowest was the 11.2% about 2 million privatization expenses on Associated British Ports.

The question arises whether the Pakistan government can afford to pay such high amount of fees and if not, then how they can plan and manage this process. In the case of monopolistic privatizations governments have to establish regulatory bodies such as Offer, Oftel, Ofwat Ofgas and CAA and also provide them experts and professionals. There is a great need to hire or train the professional people to handle this privatization programme. Only a few people mostly non professional at existing Pakistan privatization commission, can not do this job alone it need more skilled and experienced managers and consultants.

(c) STRUCTURAL LESSONS:

In the UK utility sector, especially, the early experiences of privatization were little more than simple ownership transfer, but in the later privatisation competition was introduced through restructuring the industries pre–privatization. The UK government had already developed well designed social and physical infrastructure and well planned rural and urban networks of services, and also set out a guaranteed standard of performance for all the utilities. In Pakistan, infrastructure is comparatively less developed and poorly built. There is a shaky business culture, and the private sectors only interested in profit oriented sectors.

There is a need to develop infrastructure, not simply sell what already exists particularly in Telecoms where customers wait for years to get basic facilities. Only well experienced and well developed international partners/strategic investors can meet this challenge. The same is the case with other Pakistan public utilities; for example, more power distribution facilities are required to take electricity from the grid stations to consumers' premises as current distribution lines are not enough to meet the demand of the people. Pakistan utilities require a huge amount of investment to improve the social and physical infrastructure in the country, whereas local private enterprises are only interested in short term profits.

Therefore, irrespective of UK experience Pakistan initially needs restructuring and reorganization then move towards privatization and deregulation without repeating its own and the UK past mistakes, of privatising utilities as intact monopolies.

(d) THE REDUNDANCIES AND UNION PRESSURES

One of the major threats of the privatization is job cuts. Trade Unions are always against a privatization programme which does not have any compensative protection for workers. The British government has short and long term compensation programmes of unemployment benefits and income supports schemes so people laid off can survive without jobs. In the case of developing countries, particularly in Pakistan, where such unemployment benefits/income supports facilities are not available simply copying the UK privatization model is not an appropriate option.

Already all the trade unions in Pakistan are running campaigns against the privatization programme. As a result, if the government privatises it public utilities without compensatory mechanisms, then it will face strikes and political unrest in the country.

The UK experience shows that privatization does lead to unemployment and greater income inequality. According to Dexter Whitfield (1992) during the 1980s the rich got richer and the poor were made poorer. In the support of his statement he provided the statistical data that the number of the people living on less than half average income soared from 1.87 million in 1979 to nearly 11 million in 1987, after allowing for housing costs, and by 1987 an additional 1.87 million children lived in families with an income less than half average; about 14% of pensioners had less than half average incomes in 1979 and this proportion had risen to 25% during the late 1980s. Furthermore, around two million families in UK had their income below the income support level at the end of the last decade.

Therefore, if the natural monopolies business in Pakistan is transferred to private owner(s), and become private monopolies, the situation would get worse for poor customers, and employees because of job losses. The government has to seriously consider these matters at the outset.

(e) POLITICAL LESSONS:

As mentioned in chapter 4, privatization is a long term economic development plan which requires stable and political committed government. The British privatization programme was designed and implemented by a Tory government with full political commitment and massive majorities in the 1980s. But in the 1990s when the Tory government had a rather weak position in parliament, as compared to Lady Thatcher, it also faced problems in implementing the rest of its privatization programme, eg Post Office and British Rail, and moving towards deregulatory options.

Most developing countries, including Pakistan, are not politically stable and strong. In Pakistan, recent experience shows that there is a lack of political stability and two parties with different economic policies have alternated in power, and tried to promote their own political policies and strategies without considering the previous government's plans. As a result, little has been achieved by way of practical progress.

The key lessons in such a political situation are: a carefully planned, fairly evaluated and appropriately selected privatization and deregulation policy is necessary. It is crucial to achieve long run socio-economic objectives and to develop infrastructure by restructuring industries and promoting competition and capital extension. Moreover, an attempt should be made to create competition <u>for</u> the market not necessarily competition <u>in</u> the market, which may be comparatively easier for politically and economically unstable governments. Unlike the UK it will also be

necessary to pursue and achieve all party consensus, and union involvement, if utility reform and privatisation is to be more than rhetoric, as in most contexts, in Pakistan the political contingencies are the key to success.

CHAPTER SIX

A COMPARISON BETWEEN THE UK & USA REGULATORY SYSTEMS

INTRODUCTION

The aim of this chapter is to study and analyse the regulatory systems for controlling utilities in the UK and the USA. It will focus on issues raised by these systems and identify practical regulatory options for Pakistan's privatization and deregulation of utilities. Both the UK and the USA have been at the forefront of the privatization and deregulation policies and regulatory reforms. Both countries have the same objectives of privatization, but different routes and models. Before examining individually these systems it is necessary to explore the concepts of regulation and deregulation. The main aim is to understand whether the British regulation, price cap package is significantly different from the US rate of return (RoR) regulation and how regulatory bodies of the both countries have used these models in order to encourage competition and improve efficiency in the utilities.

Economic regulation can be viewed as legislation and government intervention to promote competition and efficiency where it is absent due to natural monopoly, whether publicly or privately owned (Foster C.D., 1992). A fundamental motive of the monopolistic utilities is to maximize their profits rather than the maximization of social welfare, and this problem plus the potential inefficiency of natural monopoly have been recognised in the institutional arrangements regarding utilities in both the UK and USA. Historically these arrangements took the form of outright public ownership in the UK, whereas in US these monopolies were privately owned and were controlled by different utilities commissions.

THE CONCEPT OF REGULATORY REFORMS

Most of the regulatory reforms in the UK and USA were established during 1970s. Regulatory reforms created some confusions about the meaning of deregulation in the British context and its relationship with liberalization and privatization policies. According to John Kay and Vicker G.

> *"The frameworks of the competition and regulation faced by existing and potential participants in telecommunications, energy, transport, water, financial services and some professional services industries are being transformed. Older informal structures have been breaking down under the pressure of powerful economic, technical and ideological forces and they are being officially dismantled. This is sometimes called 'deregulation', but that is a misleading term because as often as not new and generally more explicit regulatory structures are simultaneously erected in place of what went before. The apparently paradoxical combination of deregulation and reregulation, which is most clearly evident in financial services industry is what we mean by regulatory reform"* (p222).

Moreover, privatization of the public utilities has also been followed by regulation of price, standard of services and level of efficiency. The primary reason and objective of regulation is to promote and maintain a competitive context, and also provide the remedy for market failure because the market imperfection make it difficult for market forces to achieve an efficient allocation of resources. But it can be extended to a wide range of matters, however, such as general and sectional interests of the states and governments, without considering the other elements of the market or market failure. The other objectives of regulation are to raise the standard of products, for example, raising quality of goods and services for consumers and development of the economy in order to achieve economic and welfare objectives. The experience of both countries shows that the combination of deregulation and reregulation or restructuring of the economy characterises the process or regulatory reform.

CATEGORIES OF REGULATION

There are various objectives of regulation and regulatory reforms. One purpose of the regulation may be to promote and maintain conditions for the effective competition. Liberalization may then alter the kind of the regulation that is needed in the industries. Thus regulation can find out to use competitive incentive to encourage different regional monopolists to compete among themselves. Moreover, regulatory reforms are necessary to control the privatized monopolistic industries to protect the consumers. In the regulatory system where competition may be the only effective means to protect customers and consumers against the monopolistic power and perhaps most important means of preventing the worst excess of the monopoly.

A major distinction can be drown between two categories of regulation (a) structure regulation and (b) conduct regulation, although it is not always clear cut and they are not mutually exclusive (Majone C., 1990). John Kay and Vicker J. (1990) clarify these categories in the following way:

By "structure regulation" they mean the determination of which firms or individuals are followed to engage in which activities. Examples of this structural regulation are:

(a) restriction on entry
(b) statutory monopoly
(c) single capacity rules and
(d) the rules against individuals supplying professional services without recognized qualifications.

Structure regulation is mostly related to the extent to which enterprises operating in one regulated market are allowed to enter into the other ones. The US policy has favoured functional separation, which is an important sub set of structural regulation. By following the arrangement of its antitrust case in 1982, AT&T was required to

divest itself of its local operating companies. By contrast, the UK policy has relied on the conduct regulation in the gas, telecommunication and electricity utilities.

(a) "Conduct regulation" refers to measures concerned with how firms behave in their chosen activity or activities. The important examples of the conduct regulation are as under:

(b) price control

(c) measures to guard against anti-competitive behaviour by dominant incumbent firms and

(d) rules against advertising and other restrictions on competitive activities.

The aim of structure regulation is to create a situation in which the incentives and opportunities for undesirable behaviour are removed. As far as the conduct regulation is concerned, it addresses not the undesirable underlying incentives but the behaviour that they would otherwise induce.

Conduct regulation is also known as "directive regulation" as regulators tell the regulated industries what they have to do to achieve the regulators objectives. Until recently both UK and USA followed this categories and then moved towards more deregulatory reforms. Therefore, where, a natural monopoly or potential exists, the need for regulation increases for the protection of the customers; and where competition is poor, well organised and effective regulatory reforms can stimulate and motivate enterprises to improve the efficiency and competition.

PRICE REGULATION AND POLICY

Initially, the UK choice of price control to regulate public utilities was based on its simplicity and efficiency. Price regulation, from the consumers point of view, keeps prices down vis a viz inflation generally and increases output. It also provides an

incentive to regulated enterprises to operate effectively and efficiently. In price capped regulation, profit can only be increased through redution in the costs of operation or by increasing productivity.

There are two forms of regulation: First, RPI–X introduced for UK utilities on transfer the ownership of these industries. Second, rate of return (RoR) regulation practised in the USA utilities in order to deregulate and create competition and liberalization. The former is simple and speedy in its implementation process, where the latter is more complicated and open in its implementation process.

The UK price control regulation, RPI–X and USA Rate of Return (RoR) regulation are different in implementation. In the USA regulatory system, prices are regulated in order to give a fair and reasonable rate of return on capital. However, this form of regulation has a built–in–cost plus element which greatly diminishes the incentive for industry to be efficient. Compared to the RPI–X price cap adopted in the privatization programme of public utilities in the United Kingdom.

The trend and experience in the United Kingdom shows that RPI–X is slowing involving the USA rate of return (RoR) regulation policy. As Professor Bryan, Director General, Oftel, expresses his experience in the telecommunication sector, RPI–X and RoR are from the same family of the regulation; the only difference between them is that RPI–X is altered less frequently and only takes rate of return on capital into account as one of many factors (Veljanvoski, 1989). There is a practice, especially in the telecommunication industry and in British Gas, regarding the evaluation of performance, in terms of accounting rate of return (RoR) in various activities of these utilities along with the price cap. Initially, the Department of Trade and Industry had intention to adopt the modified American rate of return (RoR)

regulation in the privatization of British Telecom but after some debates and analysis and investigation regarding price control and industry situation, the price cap regulation was adopted in the UK public utilities.

The USA operates RoR regulation in utilities sectors and also has developed various changes across different jurisdictions and industries. But the main characteristics are more or less same as the traditional rate of return (RoR) regulation where the company files a tariff when that company decides to change its prices for the next specified period of time along with all relevant calculations; for example, operating costs and capital employed. On the basis of company's calculation, the regulator determines the fair rate of return on capital employed and the level of the tariff (Beasely & Littlechild, 1992). This structure of the tariff, which is determined after estimating the demand and revenue requirement and proper calculative analysis, aims to avoids unfairness to the consumer and the industry.

UK EXPERIENCE OF REGULATORY POLICY

Since 1979, the UK government has introduced the most fundamental regulatory reforms in public utilities. Major reforms have included the necessary changes in the regulation of product market competition and methods of regulating public owned enterprises. The motives of the regulatory reforms have been multiple and their objectives have also been varied, but the ultimate theme has been concern with efficiency and competition in public utilities.

The framework of regulation for the British nationalized industries passed through a series of changes since the establishment of these industries. The development of the control system during 1950s was based on the Labour Party's Model, known as Morrison's Model, that allowed the Board of each public enterprise to pursue strategies which were in the public interest rather than the strategies which focused

on the enterprises financial performance. In 1967, the government introduced a white paper specifying guidelines for setting prices and investment levels. All these directions were drawn from standard rules suggested by economic theory i.e. prices were to be set in relation to marginal cost and investment was to be undertaken in projects whose discounted benefits exceeded the discounted present value of their costs.

Moreover, non–commercial responsibilities were to be subjected to direct subsidy and public enterprises were required to attain specified target level of the financial performance (Bishop & Thompson, 1992). The new developments provided the basis for analysing the incentive structures connected with these different phases of control regime.

In the first phase of the UK privatization programme, when enterprises transferred to private sector eg Britoil, British Aerospace, Cable and Wireless were operating in competitive markets, regulatory reform was not a major issue. The need for reform and new regulatory bodies (regulators) arose when the second phase of privatization of public utilities was started in 1984 by selling British Telecom (1984), British Gas (1986), the British Airport Authority (1987), the Water industry (1989) and Electricity industry (1990).

The most important element of regulation in the above mentioned utilities was the adoption of the RPI–X method of price control. Where, RPI = Retail price index, "X" = Efficiency factor, is set for the specified period. The RPI–X, price cap regulation requires an arrangement of the price changed by the regulated utilities at a specified rate of "X" percent every year. In brief, a ceiling is put on the annual increase in the prices of products and services of privatized utilities. This ceiling is established at "X" percent below the increase in rate of the inflation.

The "X" is the number allocated by the regulatory bodies and remains in operation for the period of five years until its renegotiation or reallocation by regulators. At the same time, the company can make changes in some prices, if the arranged price of the specified basket of its goods and services does not increase faster than the RPI–X price cap. Thus the choice of "X" in the price control formula is naturally thought of as potential rate of improvement in the cost efficiency of regulated services.

CHARACTERISTIC OF (RPI–X) PRICE CAP

The UK method of RPI–X price control has various advantages over the US rate of return (RoR) regulation. Therefore these advantages of price cap are as under:

(a) the regulatory burden appears to be limited to checking that the price increases comply with the formula, and the danger of the capture is thereby reduced.

(b) the incentives for the productive efficiency seems good in so for as the benefits from innovation and cost reduction are related by the firm.

(c) the RPI–X price cap allows the company greater flexibility to adjust the structure of the prices within the basket and in principle there is no constraint on prices outside the basket.

(d) the RPI–X is comparatively simple to operate by the regulatory bodies and the companies. It is also more transparent and focused on parameters of great concern to customers while providing them with greater assurance that monopoly services will not get worse under the private sector.

(e) this also offers more scope for bargaining than the rate of return regulation.

At the same times, there are some points of caution in adopting the RPI–X price cap formula, especially concerning the incentive to efficiency claimed for this price control regulation:

(1) The level of "X" must be set and repeatedly adjusted to secure an appropriate rate of return, otherwise allocative inefficiency will arise from the prices being out of with the costs; there can also be political pressure from the consumers and the companies.

(2) In the case where criteria for revising "X" is not clear then this will increase the cost of capital or discourage the investment. Therefore a clear guidelines must be laid down for resetting the level of "X".

(3) The effectiveness of the RPI–X regulatory system depends on whether or not the regulator can determine what constitutes an efficient level of performance and then structure the formula in such a way that a failure to achieve efficient performance will be reflected in the basic financial indicators.

According to Veljanovski (1989) the price cap regulation has reduced the real average price of telecommunication services in the UK but in a way that suggest additional problems such as:

(a) Maximum price increases are seen as minimum ones.

(b) Uncertainty as to outcome. So for, the formula has made no allowance for the impact of increased traffic on profits. The telecom sector has boomed in recent years with the result that the profit have risen rapidly within the price cap largely because average costs in a network industry decline which can

lead to monopolistic behaviour.

(c) *The price cap can send the regulated firm the wrong signals. There can be an attempt to cut costs by reducing the quality of service. The latter has been a concern with the BT's case leading to an official investigation and a new regulation to ensure the maintenance of the quality level.*

(d) *There is nothing in the BT price formula to restrain BT from re-balancing to an unreasonable extent.*

This indicates that this formula favours the privatisers as they can make more profits at the low quality of services and even showing high prices as minimum for customers. It decreases the international prices and increases domestic calls charges which are unreasonable and unsuitable for local consumers. This price control tariff is successful only if all other things remain the same for example the quality and quantity of the goods and services i.e. number of calls, electricity and water connections and increase in number of customers with the passage of time. In the reverse case it can show very unfavourable and even drastic effects which leads to the bankruptcy and the failure of the whole industrial business. Some of these weaknesses of price control regulation have been removed to the some extent by the government through regulatory bodied eg Oftel, Offer and Ofwat etc in the later development in utility sectors, but still there are some contradictory issues between regulators and utilities and ended in courts which demonstrates a need for deregulatory reforms.

REVIEWING/RESETTING LEVEL OF "X"

The price control system is known as review of price cap formula. It can achieve by resetting the "X", which represents the efficiency factor. The primary objectives of this review and resetting are: (a) to secure a fair price for consumers; (b) to allow the utilities to earn a reasonable rate of return; (c) to provide incentives to enterprises to improve their efficiency and performance; and (d) to minimize the

burden of industry regulation. Before the flotation of a natural monopoly, all parties concerned need to take a view on the possibility of improvement in productivity and efficiency of the industry while deciding and negotiating the initial "X" level of the utilities services (Foster C.D.,1992). The setting and resetting of "X" has an important role in the public utilities regulatory regime. The first level/value of "X" is set by the government at the time of the privatization of the industry. While subsequently "X" and "K" (for water) are set by regulatory bodies after consulting, in some cases, with the Secretary of state which has the following three implications:

(1) The initial level of "X" is set as a part of the whole economic package of measures and its parameters affect the revenues, costs and risks of the privatized companies. All these parameters are clearly mentioned in the license conditions of the regulated company. So, resetting the level of "X" can only be done in the context of these parameters.

(2) The initial level of "X" and "K" (for water) are set by the government as an owner of the companies and the resetting of X or K by the regulators who do not own the shares in these companies. The regulator does not has any additional degree of freedom; for example any shift in favour of one interest group to another.

(3) The difference between the initial setting and resetting of "X" which strengthen the previous "X" and relates to the effect on the firm's share price. In the either cases such as initial and resetting of "X", it will effect on the share price and profits. However, there are many degrees of freedom in selecting the value of "X" because it is set after considering the political and economic consequences related to the company profits and customers protection.

The British Telecom has been subject to price control and setting and revising level of "X" since privatization 1984. Initially, British Telecom's price cap package was recommended as RPI–3, from 1984 to 1989. At the end of this tariff basket the Director General Oftel invited alternative proposals for the improvement and development of price structure framework of the British Telecom for the next session, changing the "X" value and time period for price control. Eventually, there was an agreement between the Oftel and British Telecom on price cap package about reduction of period and to increase the value of "X" than it was revised to RPI–4.5 from 1989 to 1991 and than to RPI–6.25 for 1991 to 1993 and then revised to RPI–7.5 (BT, 1994). In setting price an assessment is made of the likely levels of efficiency that can be obtained by the utility over specified period of time.

In the case of British Gas, the previous price cap formula was set as M = (RPI–2) + Y–K from 1987 to 1992, where,

M	=	Maximum average price
RPI–X	=	Non–gas costs
Y	=	Gas costs
K	=	Correction factor

At the end of this period, the current tariff formula was revised and reset (X=5) after an agreement between British gas and the regulator for the five years from April 1992 to 1997. The new price cap formula replaced the "Y" by the GPI–Z, a gas price index and the efficiency factor this allowed British Gas to pass through its gas cost increase into prices and the efficiency factor take account of improved efficiency as well as energy supply in order to meet the customers needs. Therefore, the revised formula is simplified as:

$$M = (RPI - 5) + (GPI - Z) + E - K;$$

Where,

M	=	Max average price
RPI–X	=	Non–gas costs
GPI	=	Gas price index
Z	=	Efficiency factor – 1%
E	=	Gas and energy efficiency services

As a result of this resetting price cap regulation has tightened the restriction on the movement of the non gas element of the price. The MMC recommended a modification to the formula from the April 1994, from RPI–5 to RPI–4, to reduce the efficiency factor and to provide some relaxation on the tariff formula.

In British Water industry, the formula which controls the charging limit is like (RPI+K+U) which is different than other British utilities in term of these (+K&U) factors. The "K" is the value set by regulator which reflect what the company needs to increase charges by over and above the inflation, in order to finance the services provided to the customers. The "U" is the amount of "K" not taken up in the previous years.

In "K" setting formula by which average prices are allowed to rise November to November basis and the RPI is design to give incentive about 33 water and sewerage companies for greater efficiency and performance. Ofwat has reviewed the charging limit in 1994 and set the new "Ks" from 1995 for the next 10 years, at the same time Ofwat can make a periodic reviews and adjustments of "K value", when and where it necessary. However, "K" is the price limit for the basket of charges which are charges for unmeasured water supply and measured supply, charges for unmeasured sewerage services and measured sewerage services, charges for reception, treatment

and disposal of trade effluent. This means that company can increase the charges for unmeasured supply more than measured supply, but the overall charges should not increase more than RPI+ K.

As for as the British Electricity is concerned, the industry has different price control regulatory systems for the National Grid Companies (NGCs), the Regional Electricity Companies (RECs) for supply and distribution systems. The first price control review was completed in July 1992 for transmission business as (RPI−0) and X=0 means that prices of the services and revenues will remain stable throughout the regulated period, neither high profits at the initial level nor lower profits with the passage of time.

Again, it was revised during April 1993 to (RPI−3) in keeping the price down to the minimum necessary to sustain an efficient business. Which X=3 means that this efficiency factor cases the higher prices and revenues at the beginning and comparatively decreases the prices for the rest of the periods as compare to inflation, but it may not decrease the profits. The price control for the Regional Electricity Companies (RECs) supply side was revised in April 1994 and revised control on the distribution side is scheduled in April 1995.

USA EXPERIENCE: RoR REGULATION

The public utilities system is comparatively different on the other side of the Atlantic. American legal, political and other administrative institutions have created various different types of the regulatory system in regulation and deregulation process. The terminology deregulation also has different meanings depending on the specific kind of regulation at the issue, but it is not, as it seems, the end of the regulation. Some authors called it "reregulation".

The USA economic regulation, typically refers to governmental efforts to control price, output, product and service quality decisions of private enterprises in an effort to prevent purely private decision making regarding the public interest. The origins of the American regulation can be traced back to the case of Munn vs Illinois during 1877. The United States Supreme Court ruled that *"when one devotes his property to a use in which the public has an interest he in effect grants to the public an interest in that use and must submit to being controlled by the public for the common good"*. In the light of this decision the right of the government was confirmed to regulate private enterprises .

Congress developed the first modern regulatory agency, known as Inter State Commerce Commission, to handle this type of problem related to private and public enterprises, in 1887(Majone G., 1990). Regulatory interest regarding the fair rate of return (RoR) on investment in the utilities was further clarified and summarised in the famous case of Federal Power Commission vs Hope National Gas Company in 1944. The Hope National Gas Company case legitimated the formula used in rate of return (RoR) regulation. The Hope case illustrated that the RoR regulation is base on the theory of cost plus, which is commonly employed in different sectors of the economy. The regulatory bodies determined the revenue required to the provide the utility a fair rate of return and then the prices can be set to regain the revenues. Therefore, the Hope case generated the cost plus formula which is as follow:

$$R = O + S(V-D);$$

where,

R	=	revenue requirement
O	=	operating expenses i.e. wages fuels and depreciation
S	=	allowed rate of return on investment
V	=	gross values of utility's property i.e. rate base
D	=	accumulated depreciation

The general principles regarding rate of return (RoR) regulation are that the company should recover its costs and the consumers should pay fair price with fairness argued on the basis of cost causation and apportionment procedures. The power of the state and the regulator to implement the RoR regulation was established by the Hope decision because it confirmed the independence of regulatory commissions from the courts. This fair rate of return regulation has a long historical development in the regulatory framework process. According to Foster D.C. (1992) the rate of return is an organising concept which has developing experience of a century. In brief, the intellectual basis of the United States monopoly regulation has had curious history and the objectives set out in enabling legislations have generally been brief and to some extent vague and ill–defined particularly until 1970s, requiring the agency to decide in the public interest for the public goods. New development about the regulation shows that the touchstone of economically efficient investment and operation is marginal cost which allow a fair rate of return.

PRACTICALITY OF RoR REGULATION

From a practical point of view, the United States rate of return (RoR) regulation is considered as the most important utilities regulation, but it has no special constitutional status because there is no longer any distinction between the public utilities and other enterprises. The Supreme Court ruled that when public interest is concerned it is not necessary to create any distinction between particular categories of industries (M.A. Crew,.1979). In practice, regulation is implemented by commissions whether Federal or State, equipped with all necessary facilities and resources to do its job effectively. The commission, federal or State, has to implement the RoR regulation and has to arrange hearings regarding utilities cases and public complaints. The commissions main goal is to prevent monopoly price and other discrimination and to allow reasonable and fair earnings to maintain quality services for consumers and ensure a high degree of public safety. Thus the regulatory

body has different sort of commands and controls to attain specific regulatory goals.

The regulators set prices for all the service industries and enterprises and also determine the revenue requirement based on the regulated enterprises costs. Once the revenues requirement is determined then the regulators/commissions set rates designed to recover, during the specified period, the amount of the revenue requirement. This type of price setting and service rate making requires a continue administrative adjustments in pricing new products, adjustments for demands factors and shortages. The regulator determines standards for the public interest and also sets minimum criteria for the standard, particularly in respect of products or services quality and production methods (Roberts L., 1989). The UK government initially focused on policy of regulatory framework to improve the quality of services and controlling prices, but later stage, as mentioned before, introduced more competition and liberalization in the industries.

COMPARISON BETWEEN THE UK & USA MODELS:

The UK and USA developed the regulatory models which have significant differences. For example a shift from RoR profit level regulation to RPI–X price level regulation would also effect a shift of risks and rewards between company and its customers. The RoR regulation assigns consumers to bear the risks of the cost increases and the rewards of cost decreases as compared to RPI–X price regulation which assigns these risks and benefits to the company. RoR regulation provides full guarantees of profits to the company's shareholders through the expansion of the rate base or by arguing regulator into conceding a higher rate of return. In the rate of return regulation the customers benefits from any reduction in cost but the firm has not any profit incentive to make it (Foster C.D., 1992). In contrast, the RPI–X regulatory system presents increases average prices, greater than specified in the price formula.

The RoR regulation is based on historic trends with consideration of historic costs and demands whereas RPI-X regulation is more forward looking, depending on the prediction and forecasting of productivity and efficiency achievements in the future. In RPI-X, the initial "X" is set after negotiation and consideration of the whole regulatory framework which shows that this regulation has more degree of freedom regarding the duration, coverage, price adjustment and competition. Of course, US RoR regulation also provides some sort of negotiation and discussion among the relevant parties in asset valuation and treatment of work in process etc, but after the decisions it seems a bit difficult to change their decision.

The important difference of the system is that RPI-X system has less pressure from the utilities and customers regarding setting value of "X" because the regulator are not suppose to provide any detailed information of their decisions about the value of "X". Whereas, RoR regulation is concerned, all the relevant information are in the public record and the US regulatory commission has to evaluate every thing and reveal the basis of the decision to the interested parties (Beasely M.E, 1992). This comparative analysis shows that UK RPI-X regulatory framework has more scope of bargaining than the US RoR regulatory system in the country like Pakistan, where it is difficult to get the consensus on a policy issue and a competent regulatory bodies can determine and implement it easily.

This development shows that UK regulation is influenced by the experience of the USA public utilities regulation but it is comparatively easier and preferable due to rate of technological change in the industries like telecommunications, electricity and gas supply.

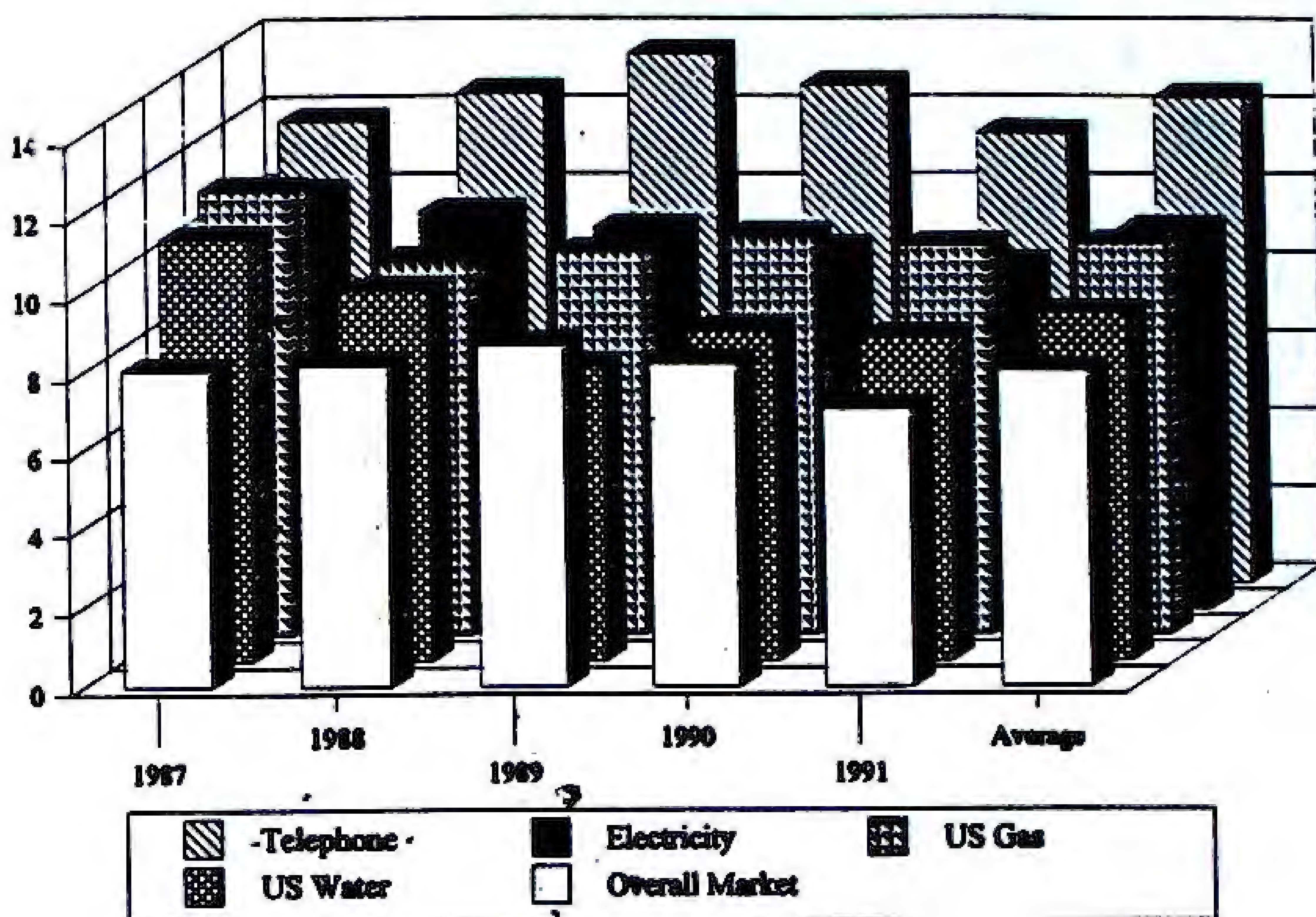
ROCE AND IMPACT OF REGULATORY FRAMEWORKS

The return on capital employed (ROCE), is profit before interest and tax as a proportion of capital employed in the business. Market based returns are interesting and informative as they include risk factors which are taken into account by the investors and provide subjective judgement in order to forecast rates of return. The accounting based measurements are less subjective and reflect actual performance and ability of the company to generate the net cash flow over time. These measurements can provide the historic range of returns which are the guidance to variability of returns experienced by different sectors of the utilities of different countries of the world.

These results and experiences in the USA and UK utilities can provide the lessons that can be learnt for Pakistan utilities especially for the telecommunication and electricity sectors. The comparative studies of rate of returns on capital employed can provide a wide range valuable indications and accounting returns of different utilities which can be relevant to Pakistan privatization and deregulation programmes. The rate of return on capital employed of the USA and the UK utilities have been analyzed. The data has been taken from Ofgas publications and developed in order to find out the impact of both countries regulatory frameworks, accounting practices and their trends. The trends in return on capital employed have been obtained which provide a better estimate of the performance of the various utilities of the USA and the UK. The following first table is showing the historic cost of the return on capital employed of the selected utilities of the USA for the last five years:

THE PERCENTAGE ROCE OF THE USA UTILITIES

Table:6.1



Source: Compiled from Ofgas reports and other sources

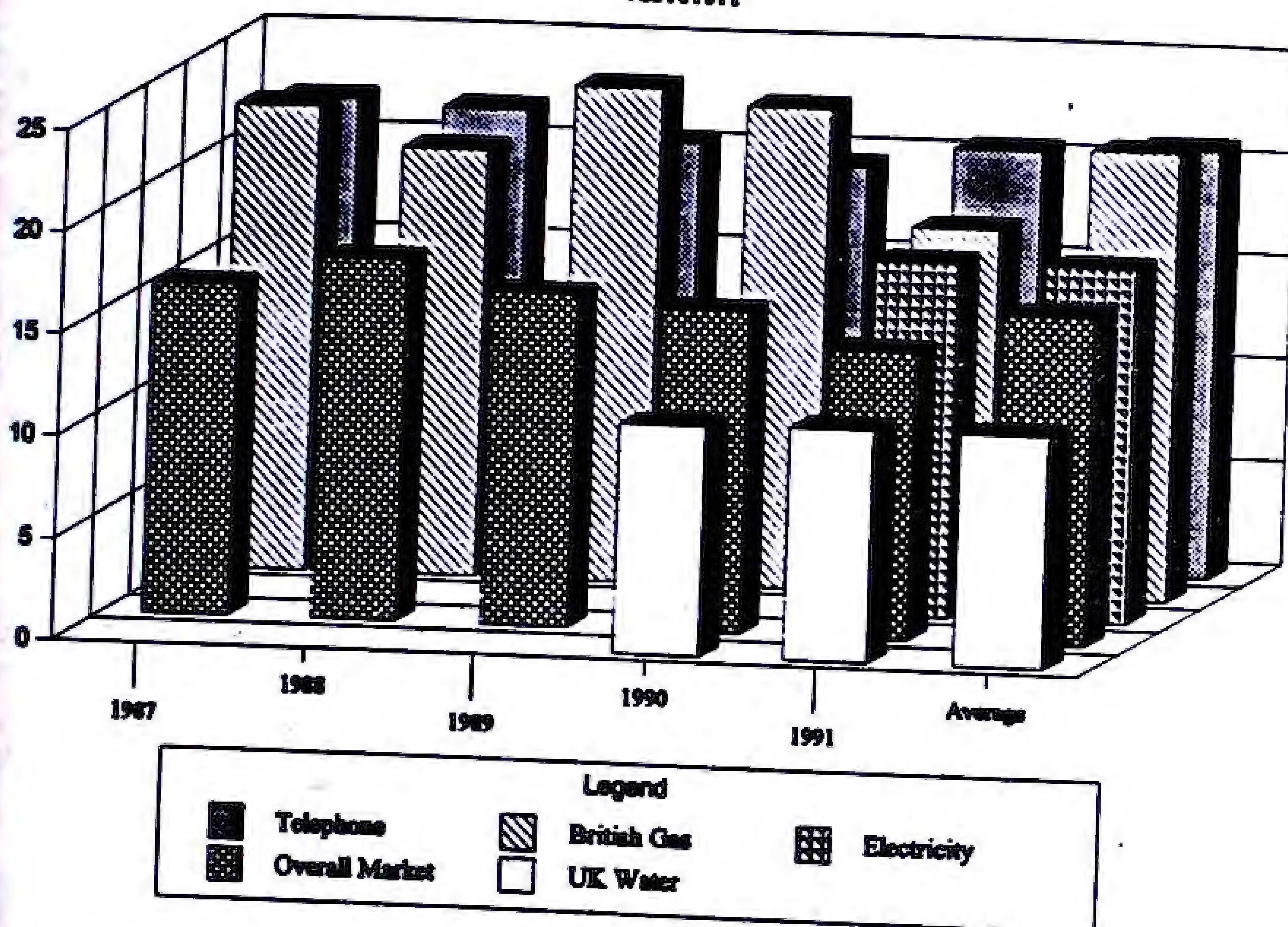
The above analysi sshows that the USA utilities which are regulated under the RoR regulation are having higher ROCE as compare to the overall all sectors market rate of return which is around 8%. The American telephone industry has comparative higher return on capital employed indicating average 12.46% than other utilities which shows approximately 9%, it is because of the regulatory environments different systems employed. The UK return on capital employed is even higher more and less double than the USA rate of return on capital employed in the utilities sector.

The following table is indicating the real comparative picture of the difference of

regulatory systems and their impact on the rate of return on capital employed:

ROCE % OF UK UTILITIES AND ALL SECTOR MARKET

Table:6.2



Source: Data from Ofgas 1993–1994

This comparison of ROCE of the both countries (UK & USA) in the above table are showing the overall UK utilities and market range of return are much higher ie about 11% to 24%, and USA range is around 7% to 14%. The British electricity and water utilities are included only from their date of privatization.

The rate of return of telephone industries both in UK and US is considerably higher than other utilities of the countries. The gas industry is second in performance

having different regulatory system in the each countries. The importance of the regulatory system and privatization models is reflected in the fluctuated return on capital, which means that the UK model is providing the higher range of accounting return because of its technical and economic structure.

In contrast, the Japanese market ROCE is 6.65%, German is 4.92%, France is 14.69% and Hong Kong market average ROCE is 10.58%. The industry share of total research and development is 76% in Japan, 65% in Europe and 69% in the USA in 1991 (Economist, January 9, 1993). These percentages show that Japan and the USA are spending higher on research and development in their industrial sectors. This experience shows that Pakistan, which has very poor consideration on research and development need to improve the managerial skills and R & D budget in academic as well as industrial sectors especially the telecommunication industry which is one of the biggest industry employing above 62,000 people, in order to plan, organize and-implement the privatization and deregulation policy effectively and efficiently for development of the national economy of the country. There is a fluctuation ROCE among different companies, overall market and countries.

This reflects different nature of industry, eg services, manufacturing or small and large business etc, and the inflation rate and regulatory system of the countries and its makes difficult to judge the real performance of enterprises.

FROM REGULATION TO DEREGULATORY OPTION:

Initially, regulation was consider as a solution to the natural monopoly issues, control of the regulatory bodies was exercised by different commissions in States. Economic regulation was introduced in US to control individual prices, output, or product quality decisions of private firms to protect 'public interest'. The Congress established first regulatory agency or commission in 1887 and introduced a series of

regulatory decisions regarding telecommunication eg 1894, 1907, 1934, 1956 and 1968. By 1960s the government regulation of 'prices' was common place in the transportation, communication, banks and utility industries. These regulatory activities were continued in various sector until 1970s. The major reasons and justifications for regulation were claimed:

(a) to control the private monopoly power

(b) to control windfall profits

(c) to correct spill over costs

(d) to compensate inadequate information

(e) to eliminate excessive competition and

(f) need to alleviate scarcity.

The UK also has historical development of regulation (UK style) of public ownership and nationalization of enterprises. By mid 1970s the deregulation movement started when evidence of a welfare maximizing orientation by the American public enterprises appeared to be weaker and having tradition being non profitable sector. As Stephen Breyer (1990) noted

> *"Beginning in the mid–1970s public dissatisfaction with many of the burdens that regulation imposed combined with economists' criticism of many specific regulatory programmes to create a strong political movement bent upon ending many regulatory programs, and reforming others...'American regulatory reforms' consist of deregulating industries that are structurally competitive. Deregulation has not meant an end of all regulation; it has typically meant removing or significantly limiting the government's power of control prices and entry, while (in case of transport) leaving intact the government's power to maintain safety. It has also meant that the newly deregulated industries have last their pre–existing statutory immunity from the American antitrust laws; now those apply to them as they do to other unregulated industries"* (p15, 19).

According to this deregulation policy, the major reforms, enacted in the mid and later 1970s and early 1980s are included:

(a) amendments in the securities Act 1975,

(b) the airlines deregulation Act of 1978,

(c) the Motor Carrier Act of 1980,

(d) the Depository Institutions Deregulation Act ,

(e) the Monetary Control Act of 1980,

(f) the railroad deregulation,

(g) deregulation of telecommunication (AT&T).

The regulatory trend (US style) came into UK as well, and started regulation of public sector and than focused on ownership transfer and subsequently deregulation and competition eg electricity and water industries, as discussed in chapter 5.

According to the Crew M.A. and Paul Kirkpatrick (1986) that *"a solution to the natural monopoly problems is deregulation. The arguments for deregulation rests on the notion that gain from the scale economies and the price control are small in relation to inefficiencies of regulation"* (p154). In support of their arguments they quoted that the deregulation approach originated in Poster's strong statement that

> *"the logical and empirical foundations of the common carrier and public utility regulations are too shaky to support further extensions...Non extension offers the most substantial prospect for the eventual elimination of regulation .. because in the long run, there may be a few natural monopolies, perhaps none, such is the pace of change in consumer taste and in technology in the dynamic economy"* (1969, p693).

Some other eminent economists and theorists like Milton Friedman, George Stigler, Averch Johnson and James Buchanan had done some ground works for the development and legitimation of the idea of the deregulation and privatization. By early 1970s much of their theoretical infrastructure for privatization had been put into practice by arranging contracting out among the local governments of the United States. However, these changes indicates the intention and deregulation movement

of the US government to reduce its involvement in the business. Deregulation of both trucks and airlines were focused on increasing competition and range of options to the public which received an active support from the eminent US leaders. The election 1980 and Mr Ronald Reagan victory marked an important change in political environment of the United States. Since then the privatization and deregulation policy became a major economic and political issue on the US government agenda and this policy as economic theory has become a political strategy and pragmatic adjustment in the United States.

The economists and policy makers have been proposed several suggestions (from regulation, reregulation to deregulation) regarding improvement of the efficiency and competition; but the final proposal and an alterative solution, they recommended to the monopoly utilities problems is deregulation and privatization. Mr Reagan government established the President Commission on Privatization (PCP) in 1987 to expand the privatization and deregulation policy, Mr Bush and Mr Clinton tried to carry on this policy with some strategic adjustments in the United States.

CONCLUSIONS: LESSONS FOR PAKISTAN

The regulation, reregulation and deregulation of USA has a long history and it was necessary especially in the private nature of monopoly to regulate the price, rate of return and the quality of products or services. Regulatory framework of UK in the monopolistic public utilities is important to deregulate and encourage competition and liberalization, but simply transfer of ownership does not make any difference as the regulatory bodies later released and introduced a deregulatory reforms and this new trend provides the lessons for Pakistan. The RPI–X price control regulatory system is well developed in the United Kingdom and Rate of Return (RoR) regulation is also well established in the United States of America. Both the regulatory Models, RPI–X and RoR, in some ways or others have some common

characteristics and features for example both regulatory systems are responsible to secure an appropriate return for the shareholders of the regulated companies in order to encourage their investment in the business. Moreover, both the regulatory systems accept the need to secure customers' needs and satisfaction of the customers but have individual characteristics as well.

This price control formula was seen very simple, efficient and having non discretionary approach which seemed to minimize the regulatory burden and protected the privatized firms from the government influence, but this efficiency and simplicity, more and less, proved an elusive in the UK regulatory system. Moreover, RPI–X regulation has unclear accountability except the regulatory watchdogs which are not fit properly in the current system of check and balance and on the other hand it is one man rules not the rules of laws (Cento Veljanvovski, 1992). The above arguments of the authors are indicating that the RPI–X regulatory framework is highly politicized, personalized, uncertain and less legalize which makes it amorphous as compare to the USA rate of return regulation. But at the same time, price control formula has commercial and industrial advantages by acting to limit the prices, through out the regulated period, rather than to limit the firms profits.

The RPI–X price control formula also provides some economic and social benefits to consumers by cutting prices of services, for example the regulated company has option to reduce charges to sell more quantity of services within its capital expenditure which even provides more revenues to it and customers are benefitted as well. There is another factor in this tariff that regulated companies can be provided a lump sum amount for the development of a specified net work, as a result the company can develop an appropriate package for its instalment, so in the country like Pakistan where labour is cheap both the firm and local workforce can be benefitted by this type of (RPI–X) regulation.

The British experience shows that Pakistan's utilities can secure a fair price for their consumers and also to earn a reasonable rate of return through efficiency and productivity and ultimately move towards deregulation option. Due to these reasons the Americans are also in favour of this style in some of their industries because of its profitability through efficiency. Pakistan has very poor consideration on research and development, need to improve the managerial skills in academic as well as industrial sectors and to motivate/educate the people for private investments. There is a need for the liberalized economy in order to plan, organize and implement the privatization and deregulation policy effectively and efficiently for the development of the national economy of the country.

At the moment, the utilities are under government influence, but the government wanted to minimize its control, but it is difficult to motivate the Pakistani millionaires, either local or overseas, to invest in the private risky business, in the case of USA rate of return model, where the investors have to invest to get the fair rate of return from the capital investments through this complicated system, therefore, there is more need to encourage and educate the investors, because of lack of private financing and potential investors in Pakistan. However, the UK and Malaysian style (BOO, BLT and ISI) privatization of utilities may be a good alternative option which is highly influence by the British style and developed by the requirement of the country in order to get involve the local and international business community in the shape of joint venture and direct foreign investments while sharing the overseas experience and know-how.

Finally, the comparative study of both regulatory experiences provide the lessons that monopoly behaviour either in private or public sector can be controlled only through competition and deregulation. These regulatory options can not be substitute for each other. The RPI-X has flexibility in moving towards deregulatory option and

competition in the market and for the market, whereas RoR is more legal oriented and complex option which is incompatible with current Pakistan situation.

Professor Littlechild (1983) states *"Competition is indisputably the most effective means.. of protecting consumers against monopoly power. Regulation is essentially a means of preventing the worst excesses of monopoly; it is not a substitute for competition. It is a means of 'holding of fort' until competition arrives"* (p4.11).

Therefore Pakistan should learn from others mistakes and of course its own past blunders and experiences, and go for gradual style competitive and deregulatory reform option with the help of highly competent and non–political personalities as a regulator, otherwise it could bring even worse consequences.

PART 3

Western British Privatization Experience & Lessons

CHAPTER SEVEN

PRIVATIZATION OF PUBLIC UTILITIES: CASE OF PAK TELECOM

INTRODUCTION

The chapter is discusses new trends and strategies for the privatization of public utilities in Pakistan and also develops the alternative options for the privatization of Pakistan Telecommunication. As industry from the Telephone and Telegraph (T&T) Department to Pakistan Telecommunication Corporation is analyzed along with examination of possible alternatives for its deregulation and privatization in the light of lessons learnt from the UK privatization programme.

As noted in chapter 3, the government of Pakistan introduced many reforms during the 1980's and early 1990's aimed at having a major impact on investment, production, efficiency, customer care and the overall economic development of the country. The government of Pakistan has successfully sold nearly sixty four percent of its targeted state owned enterprises and now pursuing the deregulation and liberalization of public utilities i.e. gas, electricity, railways and telecommunication in order to encourage the private sector. The impact of these policies on the economy can be seen through the GDP growth of the country which has increased from 4.7% in 1989–90 to 6.9% in 1993–94, and expected growth is 7% for 1994–1995.

The sales of public utilities are now a key target addition to the continued divestment of the state owned enterprises. Among the four major utilities which are now for sale, Pakistan Telecom is regarded as the best managed and most profitable utility. The government has appointed Messrs Bear Stearns of the USA and

Coopers and Lybrand of UK as the consultants and advisers for privatization of the Pakistan Telecom. Given the deregulation policy of the government, some of the telecommunications services have already been allowed to private operation, for example cellur mobile phone, pay card telephones etc. Moreover, Pakistan Telecom have approved a specification of a Telefax machine which is compatible with its network and which is being sold through the private sector. One of the biggest programmes on a BLT (built lease and transfer) basis has been taken by Sieman, Alcatel, and Ericssion for the installation of the extra lines i.e. 182,000 lines in Karachi, Sindh and Baluchistan, 123,000 lines at Lahore and 95,000 lines in Islamabad and Faisalabad. This chapter will provide an overview of the overall economy of Pakistan along with the trend and development in the telecommunication sector since the liberalization programme of the government of Pakistan. This chapter will further develop the historical performance and development of Telegraph and Telephone (T&T) which was converted into Pakistan Telecommunication Corporation during December 1990. It will facused on particularly the organizational analysis of the industry and various options and alternative strategies for the privatization and deregulation of telecommunication industry. In this case study most of the information and data were collected through field research interviews and Pakistan Telecom's annual reports.

CURRENT POSITION OF PAKISTAN ECONOMY

Hence the government of the PPP (Pakistan Peoples Party) assumed office in October 1993. The previous coalition government of the IJI (Islamic Jahmori Ittihad) was removed by the former President of Pakistan Mr. Ghulam Ishaq Khan because of the political unrest in the country. The new Prime Minister Ms Benazir Bhutto continued the industrial and economy policies of her predecessor government with some necessary reforms. The government appointed a new Chairman of the Privatization Commission and reconstituted the Commission while

merging different sub–commissions i.e. industrial and utilities etc into a one, Pakistan Privatization Commission in order to make it more effective and efficient. The main emphasis is on the development of the open market and acceleration of growth and improvement of economic performance of enterprises.

The Pakistan government views the private sector as the main instrument of economic development. The private investment has been expanded by 12% since deregulation and liberalization policy of the government, and industrial output increased by 7.3% in 1992, compare with 6.8% in 1991. The growth of the manufacturing sector reached 7.7% in 1992 compared to 6.3% in 1991 and 5.7% in 1990, and service sector growth also increased from 5.2% in 1990–91 to 5.9% in 1992. Along with the above growth, tax revenues also increased by 26% and the total revenues increased by 32 per cent in 1992 (Ben Davies 1992). Total investment increased by 17.6% and 18.8% during 1991 and 1992 respectively as compared with 10.4% in 1990 (Syed Saghiam & Doger, 1993).

As noted in chapter 3, in the air transport, four private Airlines ie the Aero–Asia, Shaheen International, Bowja and Hajewari, have started operation to compete with the Pakistan Air Lines (PIA) on local routes and Shaheen Airline has planned international routes as well. According to the Mirza report (1993), the growth of new financial institutions is remarkable during the last two years as 10 new commercial banks, 7 investment banks, 12 leasing companies and 50 Modarbas (Islamic Financing Cos) have been floated during this period.

Around 70 industrial units have been privatised, excluding 6 units in July 1994, by sale including 56 units to new parties, 4 units sold to old owners, 4 units transferred to the employees and 6 units sold to foreign companies (The Pakistan Time, February, 1993). As for as the public utilities are concerned, 10% of shares of

Pakistan International Airlines (PIA) were sold and 1% shares of PTC were sold during September 1994 for employees and general public. The power sector, gas, railways will also be privatized in the near future. As these public utilities are major sources of employment i.e. WAPDA (water and power development authority) employs 128,500 people, Pakistan Railways has 130,000 people and Pakistan Telecom employs about 62,000 people, and with privatization some of these jobs are at risk, the government has to compensate with alternative jobs and or financial compensation. At the moment, the government is introducing new self employment schemes for young people and also encouraging the private sector to invest in the different fields which will help the government to overcome the unemployment problem in the country.

The government is also trying to provide about 50,000 jobs mostly in these public utilities and advertisements were published, in the major national newspapers of Pakistan, during the first week of July 1994 to reduce the unemployment in the country. At the same time, the daily Jang London reported on 23 July 1994 that because of privatization programme of WAPDA, 8,000 workers, and 5% of the employees of Pakistan Telecommunication would be made redundant which would be a major cause of further unemployment in the country.

HISTORICAL DEVELOPMENT AND PRESENT STATUS OF PTC

The telephone utility was introduced in the subcontinent, prior to an independent of Pakistan, during the late 19th century under the Indian Post and Telegraph Department, and was developed as a successful industry. At the independence of Pakistan on 14 August 1947, the Department of Telephone and Telegraph (T&T) came into existence and inherited a small telecommunication network consisting of only 12,000 telephone lines. The Telephone and Telegraph department was separated from the Postal department in 1962 and it was attached as a department

of the Ministry of Communications. The Telephone and Telegraph remained under the Ministry of Communications until 15th of December 1990, when it was converted into a statutory corporation and known as Pakistan Telecommunication Corporation (PTC) by the Pakistan Telecom ordinance of 1990. Pakistan Telecommunication Corporation is a state owned monopoly with one of the lowest ratios of telephones households among the developing countries of the world. The government plans for privatization seek to get private capital to fund an aggressive expansion programme of telecommunication industry. The proposed privatization of the Pakistan Telecom is open to any entrepreneurs from home and abroad and investments would be fully protected by law.

As mentioned above, the industry was run by the government of Pakistan under the department telegraph and telephone (T&T) of ministry of communication. The Pakistan T&T was converted into corporation by an ordinance promulgated by the President of Pakistan, known as Pakistan Telecom Corporation Act No XVIII of 1991. Pakistan Telecommunication Corporation (PTC) owns a fairly large network throughout Pakistan, covering a total area of 803944 square kms and serving a population of about 126 million. So, Pakistan offers a large potential market for the telephone and related services. According to the PTC annual report 1992, the telephone network consists of manual, automatic and digital services, with 77,000 manual, 843,000 automatic and 555,000 digital exchange lines, but the number of telephones in operation and the registered demand for new telephone connections are almost equal. The details are shown in the following table:

THE REGION WISE MANUAL EXCHANGES

Table:7.1

Region	Exchang	Capacity	Working	Pending	Trunkboard
S.T.R.	238	17490	12342	1703	211
C.T.R.	319	2990	26558	26238	348
F.T.R	90	6934	6131	5718	76
N.T.R.	236	15189	12597	8431	142
W.T.R.	164	11390	8001	3643	60
K.T.R.	-	-	-	-	40
I.T.R.	-	-	-	-	86
TOTAL	1047	80904	65599	45733	999

Key: KTR–Karachi telecom region; WTR–West telecom region; LTR–Lahore telecom region; NTR–Northern telecom region
STR–Sindh telecom region; FTR–Faisalabad telecom region; ITR–Islamabad telecom region; CTR–Central telecom region.

SOURCE: Pak Telecom Reports and Interviews, 1993–94

As the above table shows the summary statement of manual (operated by employees) and trunk boards exchanges in the different regions of the country. It indicates that there is limited capacity,and still a large amount of demands pending. The possible solution is to encourage the private sector to broaden the telecommunication services. To date, the private sector investments have been attracted under the BOT, BLT schemes. Some foreign companies install a set number of lines at the fixed prices i.e. Alcatel, Ericsson and Siemens are installed 500,000 lines under the Built Lease and Transfer (BLT) programmes and some other contracts are under negotiation. In Mobile sector, C&W and Millicam are

also setting up a system to accommodate 35,000 subscribers by 1996 (S. Davies 1992). The detailed position of the existing auto exchanges in the Pakistan is discussed in the table below:

REGIONAL AUTO EXCHANGES IN PAKISTAN

Table:7.2

Regions	Exchanges	Inst. Capacity	Added Lines
K.T.R*	31	340,100	-
S.T.R.	58	87,820	-
C.T.R.	117	243,150	-
L.T.R.	25	205,100	-
I.T.R	13	111,787	-
W.T.R	23	37,940	-
N.T.R.	54	76,000	-
TOTAL	321	1,102,897	250,000

* Key as above

SOURCE: Pak Telecom Reports,1992-1993

In 1990 the installed capacity was 842,897 and was increased by 260,000 during 1991 and another 250,000 in 1992. The government of Pakistan is negotiating with some other international telecom organizations including AT&T of USA, British Telecom, C&W of UK and OTC of Australia etc. to develop the telecommunication system in pakistan through the BLT schemes and some of the projects are in the process. There is some opposition from the Pakistan Army which relies on Pakistan Telecom for its official communication but the government has agreed to allocate initially Rs.800 million to enable the Military to set up a separate network of its

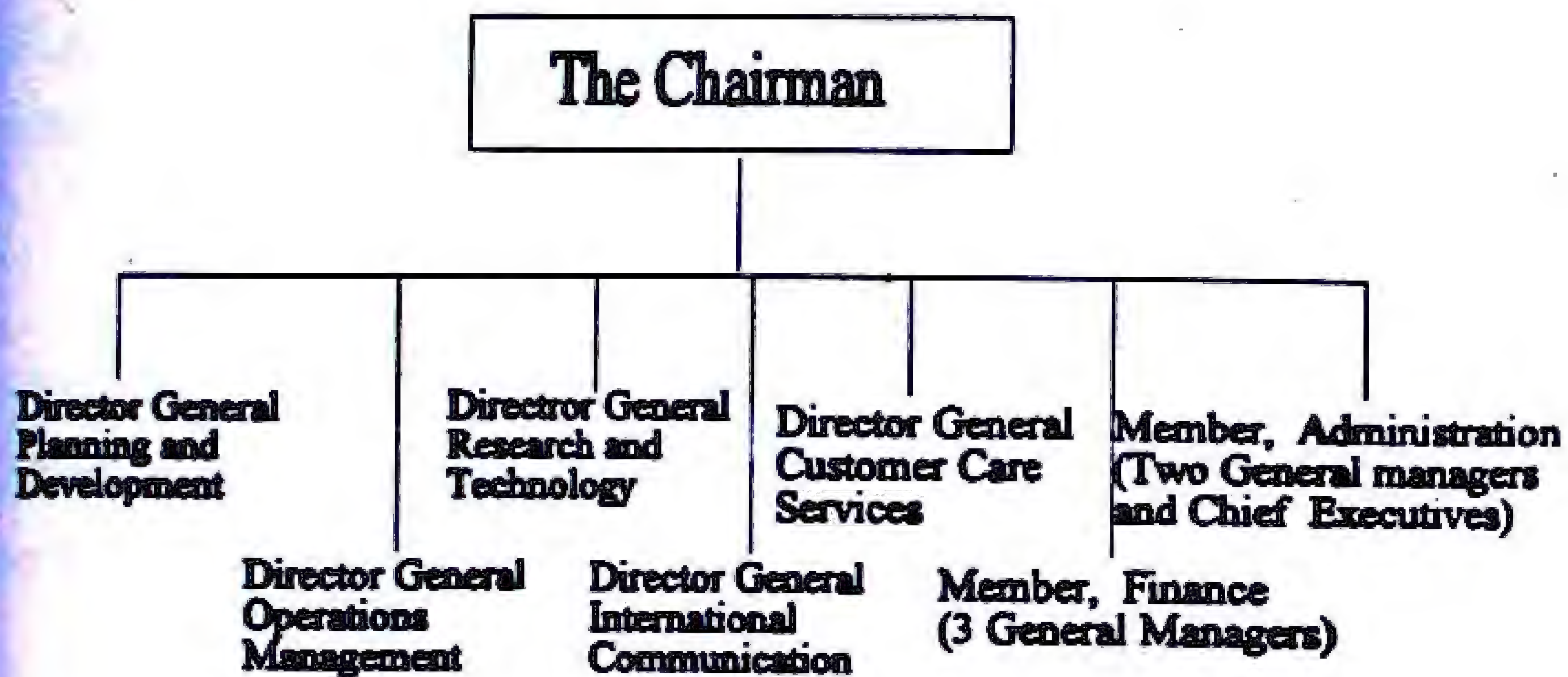
own to protect and develop its security (Salamat Ali, 1992). In the case of privatization, the employees would have one year guarantee of service with new owner and after one year they will get a golden handshake in the case of their retirement, in the shape of some specified, as at least four months salaries and a certain percentage compensation of their total service for details see chapter 3.

MANAGEMENT STRUCTURE OF PAK TELECOM

Pakistan Telecom, being a state owned Corporation, has government nominated and employed Board of Directors and administration. In light with the Corporation Act 1991, the government appointed a Chairman and eleven members of the Board of Directors. The Chairman is the chief executive of the Pakistan Telecommunication Corporation and the Chairman of the Board of Directors.

The Board is made up by the secretaries of the various interested/relevant government ministries such as the ministry of communication, ministry of finance and the ministry of planning and development, including a representative from Army (GHQ), financial institution (NDFC) and technical experts from the Pakistan Telecom itself. The general administration is headed by Director Generals who are responsible for their respective departments and are the key advisors to chairman in their areas of competence. Director Generals and their departments, performing their responsibilities under the guidance of the Chairman are as under:

PAK TELECOM MANAGERIAL STRUCTURE



Source: Developed from field interviews/survey, 1993–94

The network of Pakistan Telecommunication Corporation is divided into the nine regions for the sake of efficient operation, installation and maintenance of its respective telecommunication services. The 9 regions are again divided into various Zones which are headed by the Directors and each director controls a specified number of divisions assisted by the Divisional Engineers. The Divisional Engineer is responsible and oversees the maintenance, operation and development of the telecommunication services and also compiles the accounts for the division.

The Divisional Engineer (DE) has DDO (drawing and disbursing officer) power to draw sums of money from the authorized banks of Pak Telecom. He has to submit a report periodically to the region which is responsible for the final submission of accounts to the headquarters of Pakistan Telecommunication Corporation. All the projects from planning stage to development, are also executed on the regional

basis, so the region is called a "quality centre" and "profit centre". Some telecommunication regions are called "specialized regions" such as computer region, digital switching region, training region, optical fibre region, central telecommunication research laboratories, overseas telecommunication (i&ii), BLT regions (South and North) which are responsible for specialized and specific functions and headed by the general manager for each region.

The Pak Telecom has regionalised its network for the maintenance and operational purposes and for the development of the efficient telecommunication services. The following are the nine regions which are dealing throughout Pakistan and headed by General Manager:

THE REGIONAL NETWORK OF PAK TELECOM

Table:7.3

1	KTR–Karachi telecom region
2	Karachi telecom region–2
3	STR–Sindh telecom region
4	WTR–west telecom region
5	FTR–Faisalabad telecom
6	LTR–Lahore telecom
7	ITR–Islamabad telecom
8	NTR–Northern telecom
9	CTR–Central telecom
10	STS–Special telecom

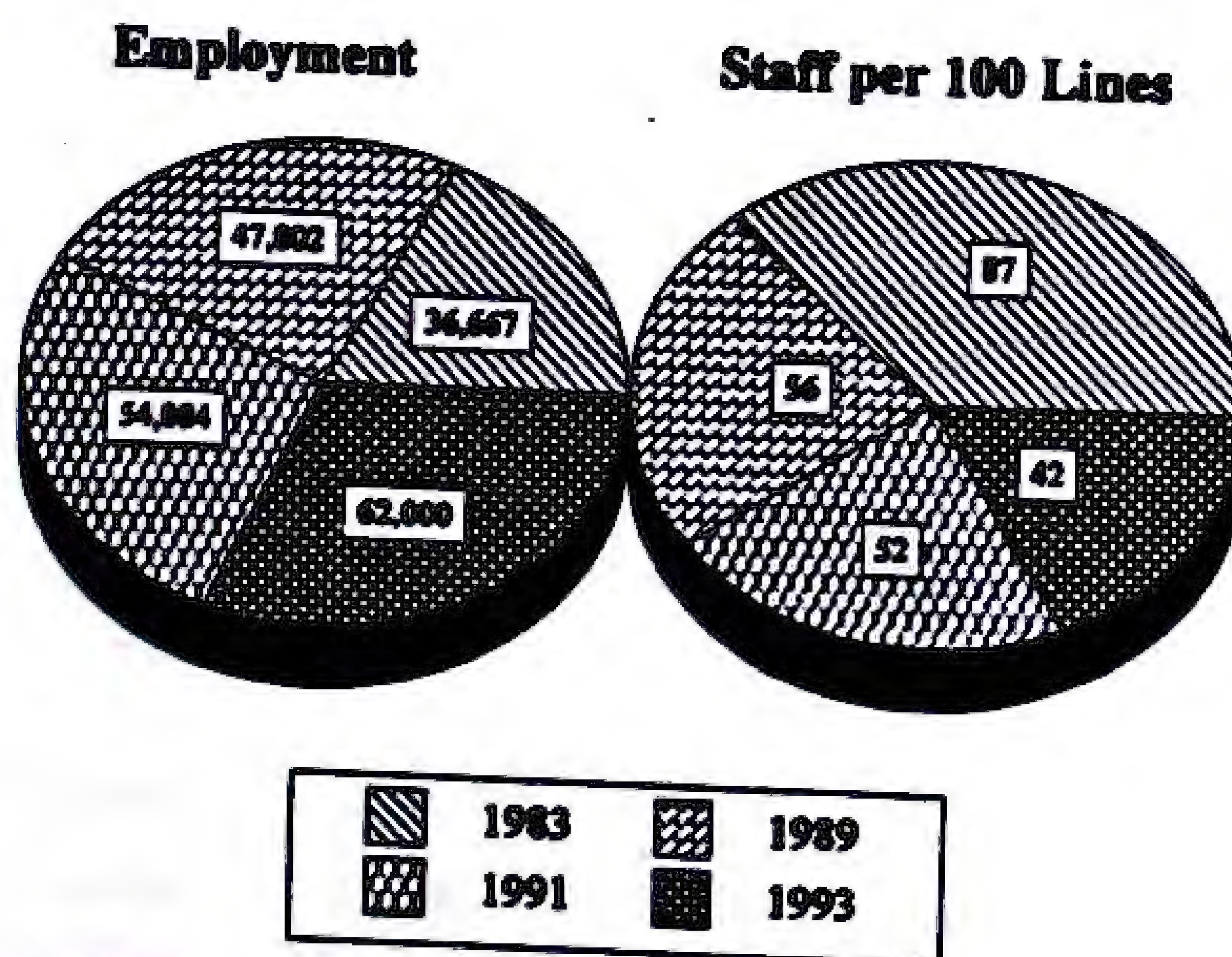
Source: Pak Telecom 1993

The above table shows the nine regions and a special telecommunication services which operates in the hilly areas like Gulgit, Sikardu and Azad Jammu & Kashmir

to provide the telephone facilities to the public and private sectors.

HUMAN RESOURCE MANAGEMENT

Pakistan Telecommunication Corporation is one of the biggest State owned organizations in the country. Being the government department of Telegraph and Telephone, the number of the employees were around 45,000 in 1988 which were considered more than enough to run the department but still there were complaints regarding the efficiency, productivity and quality of services provided by the department of T&T. When the Department of Telegraph and Telephone (T&T) was converted into corporation during late 1990, the staff was crossing the fifty thousands figure. During 1991-92, the number of the staff increased to 54,000 employees and according to the latest available data of 1993 these numbers of the employees are about 62,000. As these employment figures increased, the telecom services also increased with the passage of time and the employees per thousand lines decreased as overall gains in productivity and efficiency. According to the latest available official data of Pak Telecom, the strength of the staff from 1983 to 1993 is as under:



Source: Pak Telecom Report 1992-1993

The above data shows that within 10 years employment in the Industry has nearly doubled. There are two main reasons for this frequent increasing of staff. First, due to rapid turnover of the political administration in Pakistan as every government has tried to takean opportunity to find employment for its political workers. Second, because the Pakistan Telecom Corporation has extended and improved its range of services and it has required extra managerial and technical experts to get the jobs done.

Currently about 62,000 employees are in the Corporation and about 7% officers are in the Basic Pay scale number 16 to 22, whereas remaining 61% are non gazetted officers and workers from grade 5 to 15, including 32% helping staff of the lower grade from 1 to 4 i.e. peons and ushers. The following table shows the revenue per employee.

SALES/REVENUE PER EMPLOYEE ANALYSIS

Table:7.6

Year	Revenue (Rs.m)	Employees	Rev per Employee
1992	16780	62000	271
1991	13894	54084	257
1990	9954	49717	200
1989	8374	47802	175
1988	6549	44690	147
1987	5514	42315	130
1986	5460	41032	133

Source: Developed from annual PTC's reports

The Corporation has increased its employment but along with it the PTC has improved its sales revenues with the passage of time as the above table shows for the sales per employee from 1986 to 1992. The Pakistan Telecom Corporation has

one highest post of the Chairman of BPS22 (M-1) and seven seats of BPS21 for the Director Generals and members of the Corporation and further 34 posts are filled by the General Managers and Chief Executives of grade 20 (like full Professor) and these executives staff are 0.07% only. The corporation has employed more low grade cheap staff for operations, repair and expansion of the network which provides even more profits with higher employment with traditional operating system.

In case of privatization, with capital extension and joint ventures, these cheap labour can be utilized. The following another table shows statistics of the Pakistan Telecommunication Corporation's staff and their pay scales:

STRENGTH OF PAK TELECOM'S STAFF: BY CATEGORY

Table:7.3

S. No	Staff Category & Pay Scale	Strength	Staff %
(1)	Basic pay scale (BPS) 20 to 22	42	0.07%
(2)	BPS 16 TO 19	4080	6.60%
(3)	BPS 5 TO 15 (non-gazetted)	37,574	60.60%
(4)	BPS 1 TO 4 (lower workers)	19993	32.30%

Source: Interviews and surveys during 1994

The above table shows that the majority of the employees are in the clerical and secretaries level jobs and few of them are at top management and middle management level. This picture shows that most of them are unskilled workers. When the government decided to liberalize the telecommunication sector, the Pakistan Telecom realized the need for a proper training programme for its staff at

all levels. The government established a Post–Graduate Institute at Islamabad and developed a training management headed by the General Manager. Pak Telecom is providing training to management level at the Telecommunication Staff College (TSC) at Haripur where the University graduate engineers and College Diploma holders are trained.

PAK TELECOM RANGE OF SERVICES:

The change of the department of T&T to Pak Telecom introduced a new era of dynamic changes in the Pakistan Telecommunication sector. Pakistan Telecom provided the opportunity for the development of the telecommunication facilities in different areas. In order to improve the customer satisfaction and meet the challenge and opportunities of its new environment, a comprehensive internal reform has since been launched e.g. training package for the better human resource management, introduction of new technology and related skills which are essential for challenge of the future. Pak Telecom has also the intention to develop a social welfare scheme for its employees to encourage them to increase the productivity and efficiency.

Since incorporation, Pak Telecom has succeeded in adding about 500,000 lines to the existing telecommunication network bringing, the total number to more than 1,475,000, whereas at the inception of the corporation the total number of the lines were 977,000 and thousands of demands for telephone connections were pending (Simans Davies 1992). The pending demand due to lack of capital investment and extension programmes, makes Pakistan one of the countries which have lower than 1 main line per 100 inhabitants which are shown as under:

TELEPHONE MAIN LINES PER 100 INHABITANTS IN ASIA

Table:7.8

Fewer than 1 main line per 100 Inhabitants	Cambodia, Vietnam, Bhutan, Nepal Bangladesh, India, Sri Lanka, Indonesia, China and Pakistan
Between 1-10 main lines per 100 Inhabitants	Philippine, Maldives, Thailand, Mongolia, Korea (DPR), Iran, and Malaysia etc.
More than 30 main lines per Inhabitants	Korea (ROK), Singapore, Japan, and Hong Kong etc.

Source: Asia-Pacific Telecom Indicators 1993 & WB, 1994

The above unsatisfactory position can be improved by capital extension, resource utilization and creation of competition in the industry. Pak Telecom is arranging another addition of 800,000 lines in operation in the near future. Every 1000 telephone lines during 1993 were supervised and operated by about 40 employees as compared to 45 employees in the previous year (PTC report, 1993). The number of all breakdowns and complaints have been decreased and significant progress continued to be made in the other areas and services.

Pak Telecom owns a fairly large network spread throughout the country, operating 1650 exchanges, 500 telegraph offices and a network of open-wire carrier systems, coaxial, microwave and satellite earth stations, so its telephone network consists of manual, automatic and digital services. The overall PTC provides the following important range of services:

1 Telegram
2 Telephone
3 Telex
4 Rural P.C.Os

5 T.V. Relay
6 Inland trunk calls
7 International trunk calls
8 Data transmission

OVERSEAS RANGE OF SERVICES.

The Pakistan Telecommunication Corporation provides a modern international range of services to the customers. When Pakistan came into being during 1947, the Cable & Wireless was maintaining the international linkage/services. Initially, Karachi and Dhakka was linked with independent wireless telegraph during 1949 and later during 1950, the radio telephone link was established. With the passage of time, direct communication links were developed with the different Western and Eastern telecommunication networks on high speed telegraphy and radio telephony systems. The wireless circuits remained in operation until 1972, with the major cities of the world. After this, the telecommunication satellite brought the revolution in the telecom world. Since 1972, the international telecommunication services have grown with the high speed. As the overseas traffic grew more and more the semi and automatic ISD (international subscriber dialling) became essential for better communication services. The first international Gateway Exchange (IGE-1) was installed during July 1980 to meet the growing demand of the international calls. Now the Pakistan Telecommunication Corporation has the following overseas communication systems and sub-systems:

(1) The satellite earth station Dehmandro with DM-1A working with 60E satellite in Indian Ocean Region, DM-2B working with 359E satellite in the Atlantic Ocean Region and DM-3A is under installation.

(2) Mallach Earth station Islamabad with MLH-1A working with 63E satellite in Indian Ocean Region. Presently, these three international switching

systems on the gateway exchange.

Pak Telecom has direct satellite circuits with 40 countries, and fully automatic ISD services are provided to the 70 countries. In addition, Pak Telecom contact with the world is made through Pak-Iran microwave link recently further extended to Turkey and UAE.

A large and growing demand for both local and overseas telecommunication requires a highly reliable network in Pakistan. So, a wide telecommunication international network incorporating the highly advanced technologies was made available in order to provide the quality of services. Therefore the national and international telecommunication facilities have developed rapidly both in terms of capacity and services over the years. In 1965, Pakistan became a member of the INTELSAT and developed the first satellite earth station in 1972 with the cost of Rs.19 million. A standard-B antenna of 13 meter dais was installed at Dehmandro during 1984 to provide the satellite link with America, having 260 circuits at present.

At Malachhi Islamabad, another standard-A earth station started its operation in 1986 and now-a-days more than 330 circuits are working through it. While using these services Pak Telecom operates international Telefax and Bureaufax telephone and Telex Radiophone, Telecast leased Telegraph and Telephone along with hot-line services.

RURAL TELECOMMUNICATION SERVICES

The Pak Telecom also provides communication services to the remote inaccessible (rural) areas of Pakistan through the domestic satellite telecommunication (DOMSAT) system. Its sub-station at Islamabad is connected with small stations

in the Gilgut, Skardu and Gowader areas. For this purpose, utilizing a quarter transponder of 9MHZ capacity has been leased from the Intersat that provides 120 circuits for the above three destinations. To stretch telecommunication facilities to the rural areas effectively the time Division Multiple Access (TDMA) system is being installed to connect more than 3000 village around Larkana, Faisalabad and Peshawar etc.

Overall, transmission spread throughout the country is dependent on the number of analogue digital microwave and coaxial cable system which are being replaced by the fabric optic system on a large scale. The similar links for the inter exchange working in large cities are being introduced as to improve the quality of services.

MANUFACTURING SERVICES

Pakistan Telecommunication Corporation, mostly, uses locally manufactured equipment of telephone switches and carrier system. It owns two manufacturing factories, one is the Telephone Industry of Pakistan (TIP) at Haripur, established in 1952. This factory is a subsidiary of Pakistan Telecommunication Corporation and employs around 4000 people and produces with international standard of about 300,000 telephone sets,120 digital lines, 50,000 EMD lines (Edel Metal Dehwahlar) known as electronic mechanical exchanges, 10,000 PABX lines (private automatic branch exchanges) per year.

The Telephone Industry of Pakistan (TIP) also produces teleprinter machines, typewriters and the electronic components with high quality control at various stages of production. The TIP has recently set up production facilities for digital switching equipments.

The second factory is Carrier Telephone Industries (CTI) at Islamabad and

established in 1971. The CTI is specialized in the production of electronic transmission equipment with the concentration of high technology equipments. It is developing the digital lines at Islamabad in collaboration with ALCATEL. The Carrier Telephone Industry has now started manufacturing of optic fibre transmission equipment and its involves the high sophisticated technology of electronic components. The factory is producing all the necessary equipment for the above system and has full capacity for repair and maintenance of these equipments.

These manufacturing services have international standard of quality control and meeting not only the demand of the Pakistan Telecommunication Corporation but also fulfilling the requirement of the private sectors. There are few small factories in private sector as well which are producing drop wire, underground primary cable, underground secondary cable and self supporting aerial cables etc. Another modern factory is being established by the Agha Khan Foundation with the collaboration of Alcatal at Islamabad, Pakistan.

CUSTOMER CARE PROGRAMMES

Pakistan Telecommunication Corporation has designated different customers services centres, to serve as a one window operation for the general public, and it has extended this further with introduction of the customer care programmes throughout the country. It has always been the endeavour of Pakistan Telecom to extend the best of technical and other administrative public services to its customers after corporatization.

Pakistan Telecom Corporation also introduced Digital Switch boards at 14 stations in order to help in completely replacing the manual trunk exchanges at these stations to improve the services quality of operator assisted calls. The Introduction of the

digital switch board has provided operator trunk dialling services to more than 200 main cities of the country on NWD, net work directly. Moreover, all the booking and enquiries are completed at these stations. The system engineering for all these Digital Switch boards was designed and carried out with the technical assistance of the Siemens Engineers. The Corporation has introduced uniform codes of two and three digits for the Ambulance, Airlines, Railways, Fire brigade and Police etc., in keeping with the government policy to provide all these services to the general public. These uniform codes can provide the quickest services in all emergency situation and such services are being allowed free of charge, especially, Ambulance, Police and Fire Brigade. Various steps have been taken during the past but, now the corporation moved some steps further with the modern package of services through these centres. In order to make more effective customer care programmes, the following services are provided at each customer service centre:

- Information related to telephone and telex services.
- 24 hours local and international telephone and telex services.
- All the payment of bills, fees and demand notes at the same place.
- All corrections regarding past and future payments, adjustments and overpayments.
- The arrangements have been made for the issuance of computerised duplicate bills for telephone and telex services instead of manual bills.
- The restoration of the telephone and telex after disconnections because of non payments of bills.
- The rectification of technical faults and provision of spare telephone sets.

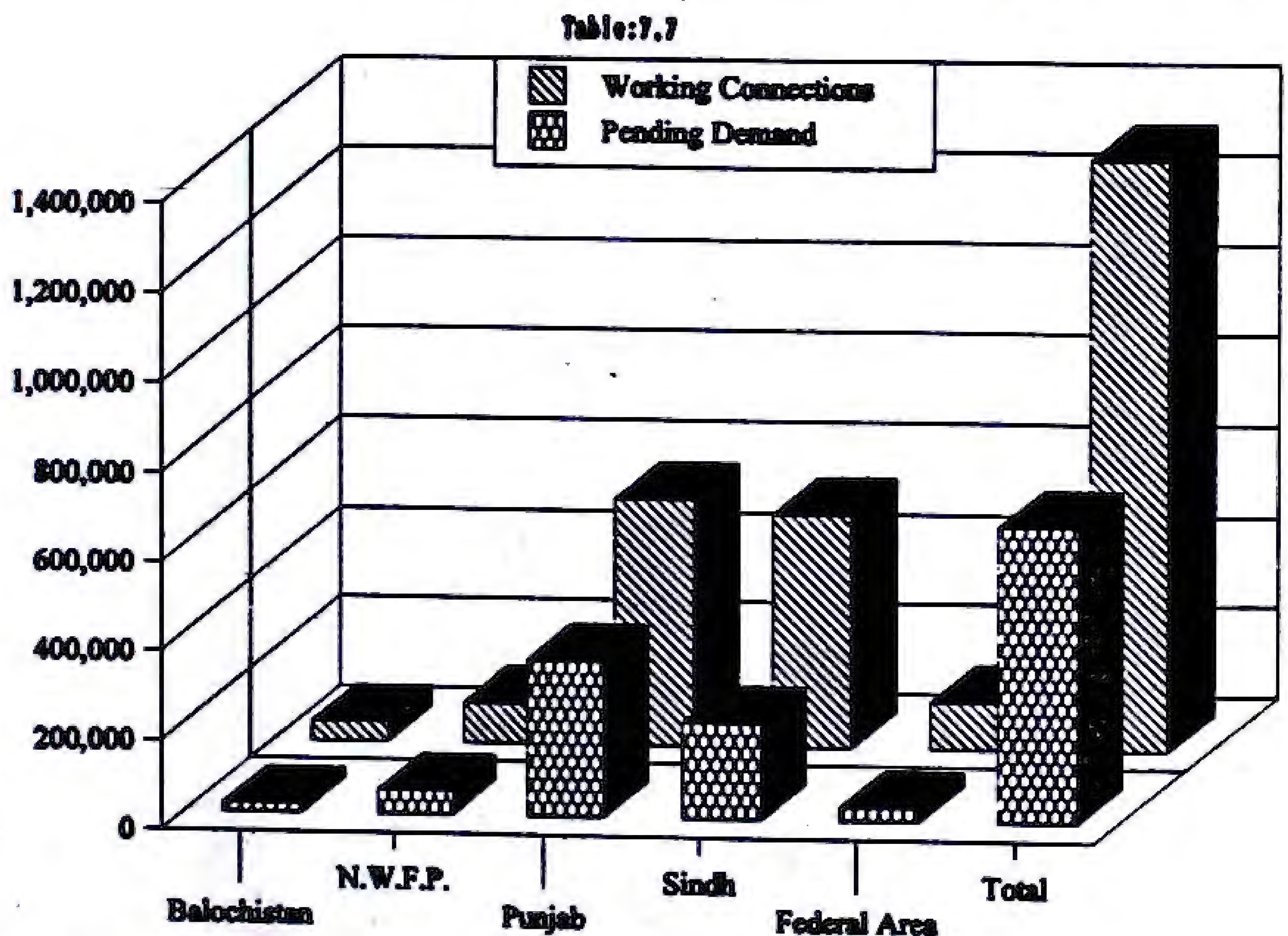
The customers can also get telephone directory and also relevant registration forms from these centre, instead of visiting to the Head Office or telephone exchanges.

CURRENT POSITION AND PENDING DEMANDS

After corporatization of Pak Telecom in 1991, it has improved its installation capicity and range of services. Now Pakistan Telecom Corporation (PTC) has 3 international gateway exchanges along with about 2550 circuits with 4 international, 4 the domestic satellite earth stations and 3 packet switching exchanges. Moreover, the Corporation has coaxial cable length of 2,322 Km Microwave route length of 6,445 Km and optical fibre links length of 1,955 KMs. Despite these facilities and capicity, stil PTC has substentioal demand for services. The details of 1990-91 working telephone connections and pending demands are given in the following table:

CURRENT CONNECTIONS AND PENDINGS DEMANDS

Table:7.7



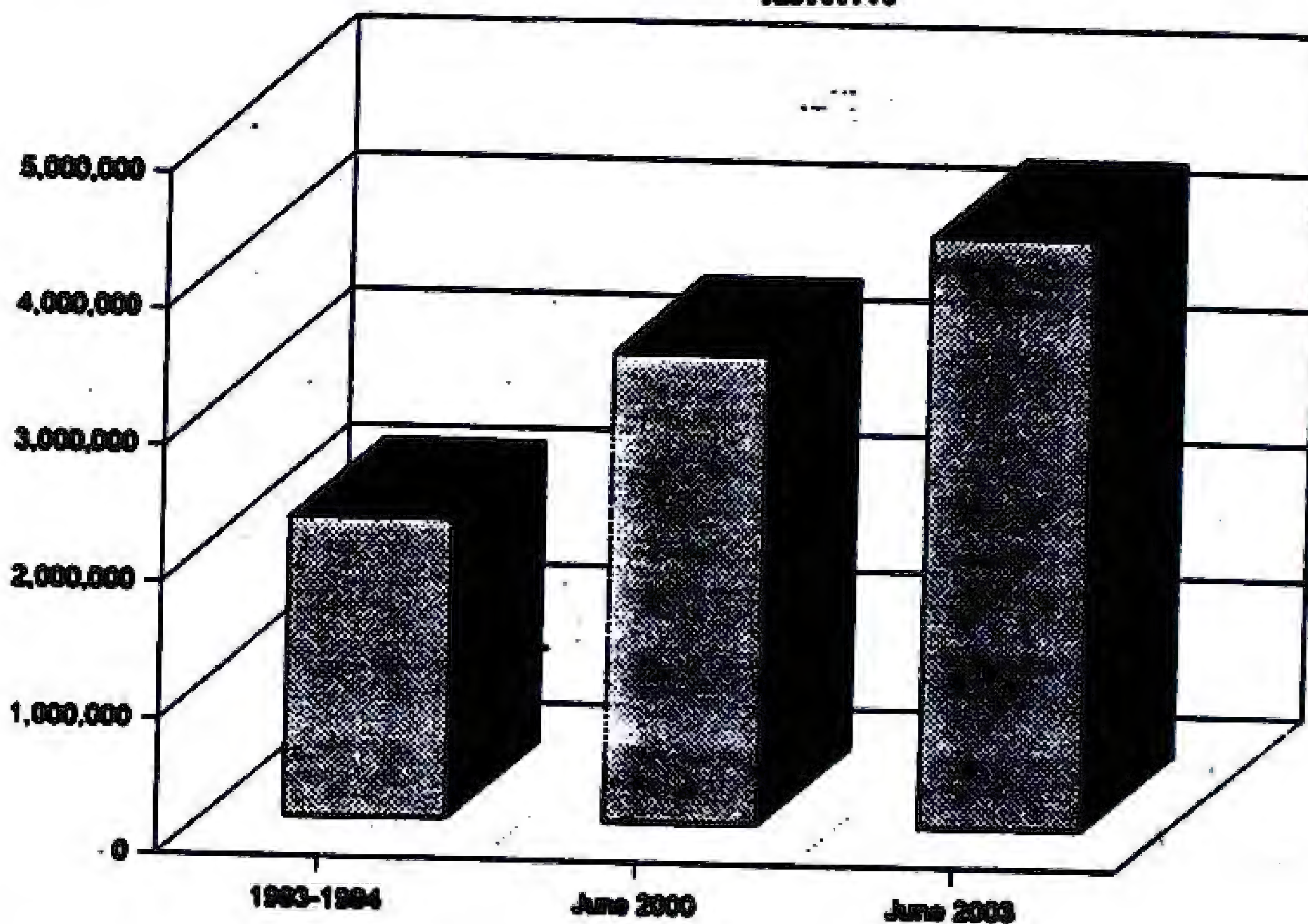
Source: PTC Annual Report, 1992-1993

Pakistan Telecom made a dynomic growth of activities in its period of Corporation couple with congestion caused due to the high valume of the overseas trafic on existing satellite channels. Therefore, Pakistan-UAE submarine cable system was introduced, comprases 1177 Km of cable across the Indian Ocean having its terminal stations at Karachi and Fujairah. Currently, the system is loaded with 6 super groups for United Arab Emmarat, Bahrain, Qatter and USA working 201 channels from Karachi and 91 from the Federal Capital Islamabad.

This sub-marine cable system is a remarkable example of the joint venture among Pakistan and international companies. During 1992-1993, the PTC succeeded to add records lines to meet their target of 2,200,000 lines.

According to a studies conducted by the USA Experts for the Pakistan Telecom Corporation, the demands and the projected growth of the telephones connections in Pakistan will rise up by 2003 as follows:

Table:7.8



Source: Pak Telcom report 1993

Therefore, the supply and demand from June 1990 and June 1993 was scheduled to insure availability of the telephone to meet the demant of the general public. It was estimated during the last year that the total requirements of the telephone connections would be more than two million, the details of the scheme was as under:

PROJECTED SUPPLY AND DEMAND OF TELEPHONES

Table:7.9

Demand	Pendings	Availability	Connection
Existing-1990	843,000	Exist.1990	843,000
Regted, demand	750,000	Add. lines	250,000
Add. demand	-	" June,92,	250,000
June, 1990-1993	410,000	" June,93,	200,000
New Lines	-	BLT schemes	500,000
Total demands	2,003,000	Exist. lines	2,043,000

Source: Pak Telecom Report,1992-1993.

But at the end of the 1993, the government could not meet the demands of the connections, what they target for 1993-1994 is still behind schedule. So, today Pakistan has less than two telephones for the 100 inhabitants. The world ratio is 9.35 telephones for 100 inhabitants, whereas Asia has 3.27, Africa has 1.22, USA 52.66 and Europe around 23.42 telephone for 100 inhabitants (The Jang 28 July 1994). Overall, Pak Telecom Corporation has very strong financial or balance sheet position which is showen in the following table:

PAK TELECOM'S POSITION AFTER CORPORATION (Rs.m)

THE ASSETS = EQUITITY & LIABILITIES

Table:7.10

Fixed asset	40736	59%	Equity	46461	94%
Other asset	17130	25%	LT Loan	2797	4%
Current "	10679	16%	ST Loan	1287	2%
Total asset	68545	100%	Cap&Resr	68545	100%

Source: Compiled from the Pak Telecom data 1992-93/ Appendix 8.7.

FINANCIAL PERFORMANCE AND ANALYSIS OF PTC:

For the purposes of analysing the Pakistan Telecommunication Corporation we decided to judge the organization through the analysis of its LIQUIDITY position, long-term STABILITY and to date PERFORMANCE with the help of the following financial indicators or ratios. This will help us to find out the real position and current situation of the Pakistan Telecommunication Corporation. Therefore the analysis can be done through the following relevant ratios:

ANALYSIS OF LIQUIDITY POSITION (RS. IN MILLION)
CURRENT RATIO = CURRENT ASSETS/CURRENT LIABILITIES

	1992	1991	1990
10,679/1,287; 10,784/1,055 and 6854/898	8.1:1	10.2:1	7.6:1

ANALYSIS OF PERFORMANCE/PROFITABILITY

Table:7.11

RETURN ON CAPITAL EMPLOYED(ROCE): Profit Before Tax/Capital * 100			
	1992	1991	1990
11597/68545*100; 9297/62394*100 and 5712/46547	16.92%	14.90%	12.27%
(i) RETURN ON LONG TERM CAPITAL EMPLOYED: Profit Before Tax/Loans+Capital(shf)			
11597/68545+2797*100; 9297/62394+2797*100 and 5712/2403+46547*100	16.30%	14.30%	11.67%
(ii) RETURN ON LONG TERM CAPITAL: Utilization Ratio*Profit Ratio*100			
69%*.334; 67%*0.339 and 54.34*0.348	23.05%	22.71%	18.96%
NET PROFIT PERCENTAGE: Operating Income/Sales Revenue			
11597/16767*100; 9297/13894*100 and 5412/9954*100	69.00%	67.00%	54.37%

As the above profitability ratios analysis indicates that Pak Telecom has shown rapid performance and enjoying highest ROCE and net profits.

THE DEREGULATION POLICY

Pakistan Telecommunication Corporation, at the time of the Corporatization, inherited about 900,000 telephones from the government Department of Telegraph and Telephone (T&T).

After Corporatization PTC has taken various important steps towards the

deregulation and liberalization of the telecom services and manufacturing of the telecommunication equipments. Some short description of measurements and achievements to date are as under:

Pay Telephones

Pakistan did not have pay phone facilities, until early 1990s whereas public pay phones are the necessity of modern day life. Everybody needs to keep himself and herself in touch with home and office, as the public call offices are also limited in number and having a long queues and only be utilized with the assistance of its operators. Pak Telecom alone was not in position to provide this facility to the public. Therefore the government liberalized its policy and allowed private companies to install and operate the public pay phones in the major cities of Pakistan.

As a result four private companies including the Pak Telecom Foundation, Telitip, Phonecard and Telecard have started work on their projects and pay phone booths are in operation in the some major cities i.e. Karachi, Lahore, Rawalpindi and Islamabad. Each licensee is required to set up at least 250 pay phones in the first year of his franchise. Pak Telecom is providing them the requisite number of lines on the priority basis and the phones are card operated only, there is no need to carry coins. During June–July 1994, study tour, I got opportunity to speak with the sales managers of these private companies which have direct competition among each other and PTC as well and they are growing rapidly and enjoying good profits.

Cellular Telephone

The Government of Pakistan has given license to three private companies i.e. Paktel, Instaphone and Pakistan Mobile Cellular, to establish, operate and maintain the modern cellular telephone services. This telephone is very convenient because

the cellular subscriber is never out of touch with his families, offices even for the movement either in the car or in the parties. These companies, particularly two of them have started their services in the major cities of Pakistan such as Islamabad, Lahore, Karachi, Quetta and Peshawer. The days are not away when whole of the country will be operated by this service. There are more than 20,000 Cellular subscribers in the country and the numbers are increasing day by day.

Paging Services

Since August 1990, Data Management, a private company, has been operating paging services in Karachi and Islamabad. This is a speedy and economic way of keeping in touch with friends at offices and homes. There is a central monitoring office which keeps track of incoming calls and delivers the message to the pagers. There is also a good market for this service and the government is inviting the local and international parties who are interested to establish and operate these services in the rest of the country.

Telecommunication Equipments

Pakistan Telecommunication Corporation had monopoly position in telecommunication manufacturing and supply of equipments. But this monopoly now has been broken and Pak Telecom has invited private companies to produce the telecommunication related products. The Fax machines and Telex machines have also been deregulated, but only Pakistan Telecom still approves brands for the compatibility purposes. There has been increased the demand for the city telephone directories due to the increase in subscribers in the big cities and the private parties are producing up dated telephone directories for the major cities of Pakistan to meet the demand of the public. In the PABX system, seven private companies are engaged in the production of the Private Automatic Branch Exchanges to facilitate the services. The Agha Khan Foundation for Economic Development with the help

of Alcatal of France has set up a factory in Islamabad, which is producing 120,000 digital telephone lines per year and Pakistan Telecommunication Corporation has a 10% share in this production unit.

There has been a ban in the import of Radio equipments before August 1990, and now these multi-channel equipments for the long distance PCO's can be imported and operated by the subscribers. Two private companies Sipka Manufacturing and East West Systems were also issued licenses for operating this system for Taxi-Cabs in the country.

BLT Projects

Pakistan Telecommunication Corporation invited private international companies to help it in developing a telecommunication network through a Built Lease and Transfer (BLT) scheme in order to meet the huge demand of telephone connections. For this purpose, four international telecommunication companies including Alcatal of France, Ericsson of Sweden, Marubeni of Japan and Siemens of Germany have been allocated projects/contracts on the BLT scheme and these companies have to provide nearly 500,000 lines within a specified period of time in the major cities of Pakistan. The details are as under:

THE BLT PROJECTS OF FOUR COMPANIES

Table:7.12

Karachi	162,000
Lahore	123,000
Islamabad	50,000
Faisalabad	45,000
Multan	25,000
Gujranwala	15,000
Peshawer	13,000
Hyderabad	10,000
Quetta	10,000
Sialkot	10,000
Sergodha	8,000
Jhelum	5,000
Gujrat	6,000
Okara	5,000
Jhang	5,000
Bahalpoor	5,000
Sheikhupura	5,000

Source: Privatization Commission of Pakistan 1993

DISCUSSION AND CONCLUSION

In the light of the above Pakistan Telecom Corporation performance analysis, it is clear that Pak Telecom has used its resources increasingly efficiently to provide the facilities to the customers as well as to earn a reasonable rate of return from its investment. Pakistan Telecommunication Corporation's Profitability ratios are constantly very high which are indicating that the higher the ratio percentages the better the performance. The profit margin of Pak Telecom before corporation was 54.37% during 1990 and it increased up to 67% in 1991 and even further increased during 1992 to 69% which very high and looks too good to be true. The return on

capital employed (ROCE) also increased by 5% after corporation; and return on long term capital employed improved too from 11.67% to 16.30%. All the other secondary performance indicators show improving trends. There seems a little doubt in the utilization ratios which are quite low in percentages which may be due to the nature of the business or may show the weakness of the present administration for utilization of all available resources of the corporation.

These utilization ratios were also very low when the corporation was a department (T&T) of the government e.g. the asset turnover was 0.214 in 1990 and reached to 0.245 during 1992. Moreover, the sale:net asset turnover decreased from 0.348 to 0.334, which again shows a clear gap of performance and efficiency of the corporation management which provides a positive sign to the government for the privatization of corporation.

The sales and profit analysis (see Appendix 7.5) and interpretation of the financial statements of the Pakistan Telecommunication Corporation shows the latest position and the current situation of the said Organization. The key indicators like Current and Acid Test Ratios are quite strong i.e. 8:1 and 6:1 as these are even slightly reduced than before. The account receivable period is also reduced from 15 weeks to 13 weeks. The stock holding periods of the corporation has also increased to meet the demand of the customers and gearing position is decreased up to 4% which shows the less long term loans payable by the Pak Telecom. The return on capital employed has also increased from 16% to 18% during 1993.

Apart from above financial position, the "Time-Series Analysis" (see Appendix, 7.6) shows a very clear pre and post position of Pakistan Telecommunication Corporation. The trend in sales increases 18%, cost of sales 29% and profit about 13% after corporatization of T&T Department. The overhead expenses remained

almost the same, but 3% increase in operating expenses and some reduction in administrative expenditures. During 1992 the long term loans has decrease by 1% from 5% to 4% and net assets has been increased by 11% from 62% to 73%. The improving productivity, financial position, labour discipline and less drain on public budget shows a good sign and strong financial position of Pak Telecom Corporation but still the industry requires new technology, capital extension and deregulation to further improve the quality and quantity of services rather than simply ownership transfer without proper competition. This analysis of telecommunication industry will provide a clear picture to the new investors and policy makers to make the right decision at the right time for the betterment of the industry and economic development in Pakistan.

CHAPTER EIGHT

OPTIONS & MODES OF PRIVATIZATION FOR PAK TELECOM

INTRODUCTION

Privatization as a major instrument for socio–economic development can be achieved through the various modes/methods. Before considering different routes and alternative options of privatization for Pakistan Telecom, it is important to clarify the policy of Pakistan government regarding privatization with reference to public utilities. The governments of different political parties in Pakistan have had different strategic views about process of privatization, deregulation and liberalization.

The present Pakistan government's priority is basically not different than the British ie to sell public assets to generate capital. This policy, however, may not be strategically suited to Pak Telecom due to the lack of domestic buyers for a huge utility. Selling the strategic enterprises to foreign investors may cause conflict at a social and political level. The recent award of 16 contracts to US investors in the energy sector have been highly criticized by the opposition groups. The opposition groups are not in favour of giving control of the sensitive utilities to foreign investors. Their point of view is that foreign investment should be welcomed but not at the cost of the security or ideology of state.

CLARITY OF THE OBJECTIVES

The privatization process is only one part of a long term socio–economic development programme and self–reliance strategy for Pakistan. The privatization objectives of Pakistan governments to date have been only short term, not least in

part because of rapid turnover and short life span of recent administrations. Every government of Pakistan has had its own objectives and priorities, which have often been unsuccessful because of frequent change in government especially for the last couple of years. Due to instability and short tenure no government was in position to make long term policy decisions and implement them. All the policy decisions and planning programmes were cancelled or their introduction delayed by every predecessor/successor. Therefore every government attempted to set privatization objectives and policies, but left them incomplete or in the planning process.

Under these political and economic circumstances it is not advisable to simply copy the policies of western industrial countries. The philosophy and experience of privatization shows that it should be particularly tailored to the political, economic and cultural environment of the country involved. It is extremely important, therefore, to critically examine, seriously plan and thoroughly analyze the various options and modes of privatization which suit to socio-economic environment of the country.

In designing a privatization programme it is important to be clear what privatization is intended to achieve. Key strategic choices must be made about objectives and priorities and the options available for achieving them. Strategic priority may include competition generation, ownership transfer, capital extension etc and each of these has range of implementation options. For example if the strategic priority is ownership transfer we can distinguish "receipts maximising" options e.g equity sale by tender, from "capital market extending" e.g discounted fixed price flotation, and "Wealth diffusing" options such as voucher system or give away. Therefore, "privatization" is not a single policy per se, as it can reflect and encompass a range of distinctive policy options. Below we analyze the privatization possibilities for Pak Telecom by identifying the distinctive policy options available and the

modes of privatization associated with them. This provides a classification by strategic purpose, rather than methodology or mechanism, which is the approach adopted by most published typologies of privatization.

The selection of option(s) totally depends on the government objectives and priorities. As noted whatever the strategic policy, there are a range of modes to achieve the objectives of the government. Therefore, a mode is a mechanism, a designed way to achieve deregulation and privatization after clarification of objectives.

The option or options can chosen according to political, social, cultural and economic priorities of the government. The government has to adopt a privatization option or options with full clarity of objectives and political commitment. Each option and relevant modes are discussed as under:

PRIVATIZATION OPTIONS REFLECTING DIFFERENT STRATEGIC OBJECTIVES AND PRIORITIES

Table:8.1

(1)	Preparation i.e. Management Reforms Option
(2)	Competition Creation e.g. Deregulating Industries
(3)	Capital Extension e.g. Joint Ventures/BLT/BOT/BOO
(4)	Ownership Transfer e.g. Over–night or Gradual
(5)	Mixture of the above Options

(1) Initial Preparation

The preparation option is an initial step towards the main objective of privatization. With this the government seeks to change the current position of the enterprise eg

if it is under the direct control of central government department or ministry or part of a specific department, then the government may change its legal status and management structure. This has been done in the telecommunication sector of Pakistan and has nearly completed its initial stages. This option is generally recommended for big enterprises or those who are not performing well, and it can be achieved through the following modes:

Mode (a) Corporatization/Parastalisation

By changing the legal status of the organization government authorizes it to be recognized in law as an independent single entity. The corporation can thus becomes independent in managerial decision making and government has less direct control in administrative matters, so the enterprise has to develop business strategies with reference to its own objectives. This change of legal status is to break up the hierarchical control of government departments and to create an autonomous, but still accountable entity. The government of Pakistan has changed the legal position of telegraph and telephone (T&T) from a department of the ministry of communication into Pakistan Telecommunication Corporation.

Mode (b) Industrial Restructuring

Under this mode governments restructure the organization of a particular industry prior to privatization. It may be divided into different territorial, regional, functional or business based units. The purpose of this restructuring is to extend capital and encourage competition in the industry. In some cases industrial restructuring involves breaking up into different functions and activities and offered them to an other departments or divisions. The privatization of Britoil involved the separation of the exploration and production assets of the British National Oil Corporation, from the remainder of the company. BT also experienced different industrial restructuring eg separation for post office, divided into five divisions and

then further reorganised it into three divisions (BT, 1989), in order to restructure the resources and improve the efficiency and productivity.

Mode (c) Managerial Restructuring

This mode can be developed through recruiting new blood and some functions or activities of the business can be handed over to the new managers with new targets to achieve. The enterprise, especially large organization can be restructured in a variety of ways, but most significant organizational structuring of the twentieth century is the multi-divisional, M-form (as identified by Wlliamson and Bhargava 1972). M-form is superior to traditional U-form of organization, where segmentation is along functional line and it may be effective in small companies. As Bishop and Thompson described that

> "*The essential characteristic of the M-form firm is that profit responsibility is decentralized to the level of individual product lines, individual brands, or geographically distinct markets (or to some combination of these). Within each profit centre the organization is then segmented functionally into marketing, distribution, finance etc, whilst corporate headquarters monitor the performance of decentralized profit centres, allocates resources (incentives) between them, and carries out strategic planning for the future*" (1994, p355-56).

This form was initially utilized in British Steel, British Rail, Post Office and British Telecom in 1980s. It is often difficult to transfer a public enterprise in its original structure, therefore restructuring organizationally and managerially is necessary to encourage more commercial operation. It can be achieved through introducing different incentives to the existing employees as well by revising their pay scales and bonus schemes. This reward to the blue-collar as well as white collar employees in terms of incentives also help to introduce into public enterprises a normal and fruitful feature of the private sector to improve the managerial efficiency.

Mode (d) Financial Restructuring

The major aspect of the financial restructuring is ensuring that the new enterprise has a proper capital structure and the business is financially self–sufficient. The level of capital must be adequate, if necessary should be injected and it must be ensured that debts are appropriately managed (Hyman H.J., 1988). As the government has to consider social objectives it may, therefore, offer special subsidies and other financial incentives to the service operators in those areas. This subsidisation and incentives may be in terms of special loans and favourable pricing reforms package. Moreover, allocation of the financial resources and funds to the more productive and profitable business area etc in order to fulfill public demands and industrial objectives and make utility more attractive and profitable. Before privatization the company accounts should be properly prepared by the accountants or financial advisors with necessary capital and liabilities adjustments to create an attractive balance sheet for the enterprise and motivate the investors.

Mode (e) Deregulation/Regulatory Reforms

Under this mode governments seek to eliminate legal and bureaucratic barriers to competition in an industry. The removal of restrictions on market entry is

> "*intended to increase the role of competition, and to the extent that private enterprises are successful in entering the hitherto protected markets, a variant of privatization will have occurred, even though no transfer of ownership of the assets has been involved*" (Kirkpatrick Colin, 1988, p236).

It shows that deregulation is an integral part of the current reform package which is directed to improving the efficiency of public sector because it is realized through experience that efficiency and productivity can improve more from a competitive environment than from simply changing ownership from public to private. The government may also introduce control of monopolistic elements through regulation

and encourage new investors by providing appropriate incentives to investment eg utilities in UK and USA. The main objective of deregulation is to expose an individual public or private sector organization to competition by attracting new participants into the market and restructuring existing companies into more competitive units.

(2) Competition Creation

Competition creation is a key strategic option to break monopolistic behaviour, improve efficiency and productivity, reduce labour market rigidities, and encourage private sector development. Michael Beasely and Stephen Littlechild state

> *"Competition is the most important mechanism for maximizing consumer benefits, and for limiting monopoly power. Its essence is rivalry and freedom to enter the market. What counts is the existence of competitive threats, from potential as well as existing competitors. The aim is not so called 'perfect' competition; rather, one looks for practical means to introduce or increase rivalry. The relevant comparison for policy is between the level of competition that could be created, and the present state of the nationalized industry"* (Bishop, Kay and Mayer 1994, p19).

Economists are agreed that privatization without competition makes little sense if it is to achieve these economic goals. The government needs to restructure the industry to eliminate monopoly and to encourage competition between utility services suppliers. This option can involves the following Modes:

Mode (a) Deregulation or Liberalization

Deregulation is a widely used mode to encourage competition, demonopolization and liberalization. The deregulation process implies the dismantling, wholly or partially, legal, bureaucratic and monopolistic obstacles to entry and eliminating tariff and subsidy barriers to competition. According to Domberger Simon and Piggott John

"Deregulation (or 'liberalization' as it has come to be known in the UK) places a key role upon the removal of entry restriction into the market. If the deregulated market is competitive, allocative efficiency gains can be expected."

The recent theory of 'contestable market' put forward by Baumol and his associates (1992) suggests that the removal of entry barriers will ensure socially outcomes, even in cases of natural monopoly, provided it can be shown that the monopoly is 'perfectly contestable'... Hence, equilibrium in a perfectly contestable market implies that a natural monopolist will be making no more than normal profits" (1994, p50).

It is now increasingly realized that efficiency gains are likely to occur mainly from increasing level of competitiveness rather than merely from a change in the ownership of public enterprises. Examples can be found in American, Chinese and Malaysian experiences.

Mode (b) Internal Market and Internal contracting

Under this mode, services are provided and purchased between governmental agencies on a bulk or cost/volume basis. This mode is also known as intergovernmental contracting, where one government authority may contract with another public authority or agency for purchase of services. For example, in UK local authorities have for many years made 'agency agreements' by which, a small authority can contract out all or part of its refuse collection services to the larger authority This strategy has been practised in education health service sectors as well. In this mode there is no element of true privatization in the sense of involvement in term of private capital, but charging and being charged for the services tend to introduce a more business-like relationship between public authorities or agencies as parties in the internal contract.

Mode (c) External Market Competition

Apart from the internal contracting, an alternative is to buy the services from private agencies and firms on a voluntary or compulsory basis. The UK parliament passed a legislation in 1987 to direct the local authorities to put six services out to competitive tender. This was a continuation of earlier Act 1980 which introduced new commercial obligations on local authorities. This provides the chance to utilize the experiences and services of public and private sectors. According to 1987–88 legislation, the services were offered for external market through CCT included: refuse collection, school meals and catering, management of leisure centres, vehicle maintenance and repairing, cleaning of building and offices and other street cleaning services (Thomas Ceri, 1988). In the local authority, if the internal contractor is not successful in the competitive tender bid then the contract will be awarded to an external firm or if the management decides that services are more cheaper in the external market then competition will be between outside services provider agencies. This system is being practised in British health, and local government services to enhance public value for money by enforcing competition; and forcing efficiency improvements as a consequence. It is simply the extension of the approach typically adopted by governments to large scale construction projects to a wider range of professional and administrative provision.

Mode (d) Charging for Services/Subsidy Reduction

The concept of 'commercial viability' is a move away from subsidised prices for public services towards more realistic or 'market' prices reflecting the cost of providing such services. The new trend is to impose user charges for services which have previously been funded wholly or partially through taxation. It encourages the growth of the private sector and competition in certain services. The mode is to run the industry more business-like rather than a government subsidy. One aspect of the mode is to move away from subsidisation towards more realistic

competitive prices for the services. In Kenya its called cost sharing in health and education services. Now the British government policy is move away from tax funded services to cost sharing for the services and there is a standard charged per prescription, a specified fee in higher education and dental treatment now charged 80% of cost as result more people are joining private dental treatment schemes (C. Mair 1994). This policy is controversial in Britain but does create a trend towards encouraging private sector provision.

(3) Ownership Transfer

Ownership transfer of SOEs and assets by sale to the private sector is what the most people understand by privatization. The ownership transfer option involves the disposal of assets in public firms and utilities to the private sector through trade sale or public offering (Domberger Simon and Piggott John, 1994). This policy of transfer of ownership has been the central thrust of Conservative Party in Britain, as well as of Pakistan governments since 1979. This approach was adopted in the UK and other countries to reduce the budget deficits and public sector borrowing requirements, both by removing the need for subsidies to nationalized industries, and generating the receipts for the exchequer from the sale of the state assets. The UK government has nearly completed the sale of all public utilities whereas the Pakistan government is planning to sell these public utilities (see chapter 3 & 4). The following modes can be adopted in order to privatize state own enterprises depending on the objectives of the government involved.

Mode (a) Receipts Optimization/Capital Generation

The major economic gain from privatization is the receipts or revenue accruing to the government form asset sale (Domberger Simon and Piggott John, 1994). It generates new sources of cash flow and financing for enterprises eg increased domestic investment, return of flight capital, direct foreign investment and reduces

government's fiscal deficit and its internal and external debt (Lieberman Ira, 1993). This mode of privatization is a major capital gain for government to meet PSBR. The UK government applied this strategy during 1980s for optimization of capital receipts in the utilities sector especially in the BT and the BG privatization. In this option the government may sell the public enterprise as whole or the enterprise can be separated into different activities and then can be sold with ownership transfer to a new private investor(s). The sale can be carried out by the competitive bidding as well as through the general auction or negotiation with the individual buyers.

As this mode is a major source of receipts for government to meet the budgetary deficits or to develop the infrastructure and optimize it in other welfare activities. The receipts can also be utilized in alternative competitive and profit making projects for overall development of the economy and creating employment opportunities for unemployed people. In the case of partial transfer of ownership of the utilities this capital can be used for development of the network and expansion of services for general public. This mode is equally popular in the developing and developed countries for capital generation.

Mode (b) Ownership/Wealth Diffusion

The aim of this mode is to offer shares at discounted rates or through voucher system to share ownership. The 'voucher system' is a free (or at minimum price) distribution of ownership to the adult citizens in Eastern Europe ie Poland, Czech and Slovakia etc. In these countries the free vouchers method is the only way to transfer the state property to private ownership, where the people have no enough money to buy it by cash. These entitle the citizens to bid for ownership of offered shares of SOEs (M. Mejstrik, 1993). In this ownership diffusion policy capital gain is not the objective, but priority is to transfer or give away the ownership of the state owned enterprises to the general public as policy of wealth diffusing. So

optimization of wealth is not a priority but the generation of new market through equally distribution or transfer of state assets to general public, as it has been implemented in some Eastern European countries after the end of centrally command economy.

Mode (c) Capital Market Deepening

This is another mode of ownership transfer option, where new shareholders, as government policy of wider share ownership, are encouraged through discounted fixed price floatation. As Paul Grout noted that

> *"In 1979 the proportion of the adult population of the UK that directly owned shares in companies was 9 per cent. In the last thirteen years this has risen dramatically and it is estimated that 25 per cent of the adult population now own shares"* (1994, p299).

The government can sell full or partial shares to the general public, institutions in domestic as well as international markets. Moreover, the government can allocate a certain amount of shares to employees on the discount basis and in some cases even free of cost to expand ownership and keep them happy.

The main advantage of this method is that it permits wide spread shareholding and brings the broader resources of general investors. The policy was the result of government programme to change ownership from state to general public through the wide spread shareholding (Robert Fraser 1988). This mode can be utilized in combination with above modes on an all at once or gradual basis to involve the common people in the share ownership.

Mode (d) Liability Transferring

This method of privatization can be achieved by discounted sale to interested buyer(s). The ownership can also be transferred through a management/employee

buy out (M/EBO) with give away and discounted basis to run the business for a specified period of time to make it profitable. If the government feels that it is difficult for it to improve the profitability and productivity of utility and the quality of services, then liabilities and responsibilities of the government can be transferred to capable interested groups from local and international investors, for example UK government gave PSA to TARMAC along with some compensatory cash to manage the business and jobs of the employees. In some cases if employee group have ability to run enterprise for their owned with an appropriate reforms programme then the government can hand over its liability to them with challenge and incentives. This is another way of achieving rapid injection of business skills by involving or transferring enterprise or its activities to the capable management, employees or joint partners to achieve the productivity and efficiency by transferring ownership.

Mode (e) Liability Termination or liquidation

This mode can generally be used as a final card. If the government has attempted other modes to privatise an enterprise and could not get any encouraging response, then it can be liquidated to settle the debts. Liquidation occurs where a public enterprise has done too poorly to merit continuance in its present shape and therefore treated for disposal at a distress price (V.V. Ramandham, 1988). But this mode is not applicable to Pak Telecom under the current position. This mode is being practised, where the enterprise is loss making and less demanding, and its disposal becomes essential to avoid further losses.

(4) Capital Extension

Capital extension can be achieved with or without ownership transfer. This option is quite popular in China, Japan and Malaysia, because it helps to improve competition, efficiency, quantity and quality of services. Under this option, BLT,

BOT and BOO schemes can be adopted to bring in the private capital and skills.

These BOT, BOO schemes are vary greatly and flexible to utilise, in which the investors maintain ownership of a project assets for a specified period of years or the ownership of the project can be transferred to the company immediately upon commissioning or depending on the specification of the contract. If the managing company is given full management control, authority to run and manage the business under a defined agreement, then this would be a management contract. If the manager is retained to assist the management and to advice the technical matters and professional aspects of the industry then it would be more advisory and consultancy position. In case of management contract, the managers would interested to provide the specified facilities and services as a return they would receive the fees and some other forms of compensation for his efforts and devotion.

Under this option, the main objective of the government and enterprise is to seek the experts skills to organise the industry in business like approach at the reasonable fee without bringing a manager into the equity/ownership position. These BLT, BOT schemes offer a potential of accelerating network expansion by an infusion of new capital and improved private sector operating practices. According to Smith and Staple

> *"For the state-owned enterprises, and the B-T (build transfer) is a form of off-balance-sheet financing that may avoid government controls on more conventional methods of raising capital such as issuing bonds. For investors, the schemes offer a potential to invest in a sector where there is strong growth in demand, little or limited government supervision of the delegated monopoly franchise, and the possibility of reducing costs compared to those of the state-owned operator"* (1994, p555).

If the government policy is in the favour of this option, which provides capital

injection, competition and quality of services, then following alternative modes can be considered for its implementation:

Mode (a) Joint Venture/Partnership Extension

Joint venture is a reduction in the proportion of public ownership, so that a wholly public ownership enterprise becomes partially publicly owned, or a partially owned public enterprise becomes more partially public owned. A joint venture programme between public and private owners offers management and ownership control in a specified proportion as mutually agreed in the partnership contract (Ramandham V.V., 1988). This mode is highly popular in the developing countries because it provides a rapid injection of capital, business skills and international know-how and experience. Partnership, in new equity rather than existing, either local or international, can be in equal proportion such as 50/50 or unequal in proportion such as 70/30 with majority stake of government for a specific period under a specified contract. Because of the flexibility of the mode, it can also be combined with other relevant approaches e.g. franchise and joint venture to meet the demand of customers. In the franchising arrangements, franchisee have to utilize the managerial and business skills as well as capital to use the latest technology and know-how to run the franchised activities profitably. In the joint venture contract, the parties are given full or specified responsibilities for the enterprise operation because of its professional domestic or international experience to run the same business and it looks a viable option for privatization of Pak Telecom. There are already some examples of partnership in Pakistan utility services specially in manufacturing units of electricity and telecommunication.

Mode (b) Private Venture Extension

This scheme can be arranged for a specified period of time eg build operate and transfer (BOT), for an unlimited period of time eg built own and operate (BOO)

scheme or with government as buyer through BLT projects. Under franchise agreement, the interested party get the license to provide services of the enterprises from the government to run the activities of the business for the particular period of time for the agreed payment to the government.

The franchiser has to take the full business risk and to make the compensation and payment to government, regardless of the profits or loss. Therefore private franchiser has to invest to extend the quantity and quality of services to run the business efficiently and effectively. Some projects under the above schemes ie BLT, BOT are practised in Pakistan telecommunication and energy sector. Other relevant examples are KLK interchange of Malaysia, Water in France, Telecom of Indonesia etc to involve the private sector in order to expand the services.

Mode (c) "Ownership Transfer" through Strategic Investors

This approach can also be utilized after developing an initial involvement of strategic investors as a joint venture or partnership in the big utility under a specified period of time. These strategic investors with good experience at local or international level. When government is satisfied with these strategic investors, then can transfer ownership to them. The government can sell and transfer to the existing private shareholders or by gradual disposal of the shares to the interested parties. In case of foreign investors who are engaged in the same line of business and having the special interests in the enterprise can get higher priority. One of the merit of the private strategic investors is that the prospective buyers are already known by the government and can be evaluated and selected on the basis of their knowledge and experience of the field. In case of PTC the government can get the confidence through the analysis and observations to make sure that industry is going into safe hands. The ultimate goals of this technique are to improve efficiency, corporate control and productivity. As Thomas Scott noted

"the best way to improve corporate control would be to sell the enterprises one by one and rely upon the new owners to protect their investments by establishing better management and restructuring production" (1993, p173).

This mode requires to evaluate and assess all the necessary matters before offer for the sale and it can also be adopted before or simultaneously with public offering method of privatization.

(5) Mixed Mode Strategy

This privatization option is a combination of selected modes which can be tailored with particular social, political and economic circumstances of a country. Under this option, therefore, the government can link different compatible modes especially, as policy objectives are complex and interrelated. In type of situation no single option is suffice to cover the multiplicity of objectives. Options are not exhaustive and exclusive for example competition creation by deregulation may create capital extension and equity based partnership may result in ownership transfer over time. Options and relevant modes may be pursued in a revolutionary or evolutionary way; but strategic industries typically require comprehensive planning and gradual implementation process. Slow and safe journey is preferred by every one, but speed is always controlled by the driver not the passengers. Passengers of privatization in developing countries are mostly dependent on "drivers", the donors.

POLITICAL & CULTURAL ASPECTS OF MODES

The range of options and modes shows that each and every area of public enterprises and their activities are open to various combination of the above modes of privatization depending on the particular interests and objectives of the government. Choices have to be made among the options and related modes before the implementation of the programme and these choices must take account of

contextual factors. Developed countries such as France, Japan and the UK equity floatation have expanded and developed the financial markets and also increased the number of the shareholders. This strategy can produce good results in the developed countries but its results in the developing world, where the capital markets are not strong, are doubtful (Helen Nankani, 1989). Experience shows that it takes time to develop appropriate institutions and regulations for stock market operations in the developing countries.

According to Veljanovski (1989) the choice of the privatization techniques depend upon the government's goals and objectives. Further its depend on the condition of the public enterprises, their area of activities and the social and business culture of the country. In a country like Pakistan, which has weak capital market, political instability and army views about ownership transfer etc, all these contextual factors militate against any single mode of privatization for utility service(s). There is a need to develop a practical and tailor-made approach with selected available modes which can fulfill and accommodate both the government goals and the customers requirements.

The British Telecom experience shows that simply ownership transfer could not achieve the desired results because of lack of competition and Mercury the single competitor allowed proved as unsuccessful and is withdrawing its domestic services. It was been realized that the reorganization and deregulation of BT was feasible as in its first proposal. If BT was split up, then there was scope of more competition among its component parts via other contracting out and franchising arrangements (Lester Hunt and Edward Lynt, 1991). The initial policy of UK government, simply ownership transfer without competition, is now moving towards deregulation and liberalization.

In later privatization of the UK public utilities the government adopted both privatization and deregulation policy and divided the industries into different local companies in order to create competition and efficiency.

The experience of the UK Electricity, Water and Railways industries show that the government has changed and restructured privatization policies in the later development of the privatization programmes in order to break the monopoly of industries and the government has learned the lessons from it own experiences.

According to Railways Act April 1994, Railtrack, a public company, took over the Railway infrastructure and started to charge for access while all the passenger services will eventually be franchised through the new office of Passenger Rail Franchising (John Dodgson 1994). Most of the railway services in different sector will be run by private franchisers on the publicly owned network. Now the UK government is also planning for privatization of Railtrack in near future. Therefore, this new deregulation policy of the Britain is providing new experience and lessons for the privatization of Pakistan utilities.

ARGUMENT FOR MODEL: WHY MIXED MODES STRATEGY ?

According to World Bank (1992) privatization should be used to encourage competition, expand capital and control of monopolistic behaviour as ownership transfer alone does not achieve the real goal, and private monopoly is even worse. Therefore, enhancing efficiency should be the first priority which can best be achieved through competition. It can show good results if government first has liberalized and deregulated the telecommunication industry and established a legal framework through which the regulators can protect the customers and enlarge productivity and efficiency.

Due to monopoly position of Pakistan Telecom, and the political situation of the country, it is quite difficult to recommend one specific mode. The main reasons for recommendation of mixed modes privatization for Pak Telecom are:

first, as noted above the government of Pakistan has no clarity of priorities, and multiplicity of objectives, ie raising revenue, improving efficiency and competition creation, requires mix modes of privatization and deregulation;

second, absence of capital market and poorly managed stock markets can not handle this type of big utility privatization;

third, telecommunication is a highly technologically based industry which demands high skills, know-how and large scale investment which may require joint venture with experienced international investor(s) to bring in capital and managerial knowledge and experience;

fourth, local business-culture in Pakistan, which is highly influenced by government regulations and the previous poor response from local investors, because of their limited financial sources and complicated process of getting business loans and other resources from the government institutions, favour the mix modes approach. This private-public business relationship will create favourable environment for gradual privatization; and

finally, as mentioned before, the week political position of the governments can not allow them to implement a single controversial

policy regarding privatization. Pakistan Telecom is providing communication services to the Pakistan Army which will not accept total equity sale for defensive and strategic reasons and all these factors suggest that one single mode would not be appropriate for Pakistan Telecom given the position of the country and industry.

MAJOR CHARACTERISTICS OF THE 'MODEL'

One of the most important characteristics of the model is that it is designed to secure consensus/support from different social, political groups and international donor agencies. This reorganization and structural reforms of Pak Telecom corporation will create competition and improve efficiency. The employees of the Pak Telecom also require jobs security and they may interested to buy and run some of the Pak Telecom services while utilizing their experience in the industry. This new tailored 'mixed model' and its steps and stages are discussed below:

PREPARATION & INITIAL PLANNING

Privatization of such a big monopolistic utility is a very complex and lengthy process. This programme requires an appropriate planning, gradual organization and evolutionary strategy within a time-frame. The world experience shows that transition from a monopolistic public utility to a competitive decentralised system takes at least half dozen years with full political, economic and technical support. Some countries are still moving forward through trials and error while learning from their past experience. The government of Pakistan comes under the latter categories. The above model provides a long-term planning programme of preparation, deregulation and privatization through five phases, implemented over a number of years. This strategy may take five to ten years to develop significant competition and experience with the new system. This model can be implemented gradually through following stages:

FIVE STAGES OF IMPLEMENTATION PROCESS

Table:8.2

STAGE 1:	*Establishment of Regulatory Apparatus*
STAGE 2:	*Industry Restructuring/Reorganization*
STAGE 3:	*Competition Creation/Trial Franchises*
STAGE 4:	*Deregulation/Privatization*
STAGE 5:	*Joint Venture with Strategic Investors (ISIs)*

STAGE 1: ESTABLISHMENT OF REGULATORY APPARATUS

The effective implementation programme always depend on the managing and controlling authority. The government of Pakistan has to establish an autonomous regulatory body (like Oftel) and higher monopoly control commission (like MMC), under a Telecommunication Act before privatization of Pakistan Telecommunication Corporation. This independent body would have the functions, powers and responsibilities to maintain the traditional role of a "watchdog" to protect the interests of public and private sectors along with the settlement of matters concerning franchise licences, amendment of licences conditions, price control, enforcement of competition legislation, initial licence fees and renewal fees, other related complaints and grievances among the regulator, utility and consumers.

According to telecommunication Act, the post of Director General and Deputy Director General have to be created in order to advise the concerned minister on the grant of licences, modification of licences and determination of price cap regulation. As for as "price – cap" regulation is concerned, there is a full comparative analysis

of UK (RPI – X) and USA (RoR regulation) in chapter 6, which concludes that UK regulatory model is preferable in Pakistan. The Director General should be highly competent and professional educationist i.e. Prof. Sir Bryan Carsberg, Don Cruickshank (Oftel) and Prof. Stephen Littlechild (Offer), who can regulate and run the system. The DG should be totally independent from the telecommunication industry which he regulates; and, in addition, he should also be independent from government.

The monopolies control commission can also supervise the telecommunication industry regarding regulation and modification or renewal of licences including certain settlement of grievances and watch on trade practices etc. with coordination with the office of fair trading.

The administrative staff of this autonomous regulatory body should be highly qualified, professional and unbiased honest persons. The professional staff should be included: (a) accountants; (b) economists; (c) engineers; (d) lawyers; (e) managers; (f) resource management consultants; (g) statisticians; and (h) technicians. All the above staff should be hired carefully on the basis of competence rather than political affiliation. The regulatory body should be funded almost entirely from the license fees and its budget should be approved by parliament.

STAGE 2 : INDUSTRY RESTRUCTURING/DECENTRALIZATION

This phase is very important as well as challenging for Pakistan government. In this phase Pak Telecommunication corporation has to be restructured into two separate entities "Pakistan communication international" and "Army communication services", which involves allocation of assets, accommodation/settlement of employees and determination of the responsibilities and functions of each company.

This decision should be based on strategic consideration such as desire to create largely private and competitive environment to improve efficiency and quality of telecommunication services with the passage of time.

This restructuring will meet the cornerstone goals of privatization and deregulation e.g. to create competition and improve efficiency by attracting foreign direct investment (FDI) and by encouraging international joint venture. Pakistan has already business linkages with international world and there should not be such a problem. In domestic context, there might be some opposition from the social and political groups as well as from the employees. Pakistan political and organizational culture can easily lead the employee and public to strikes and demonstrations against privatization programme and redundancies of jobs. Therefore, the government must take precautionary steps and expect this type of constraints and try to tackle them in advance through corporate bargaining and mutual agreement. All these political, managerial and technical matters should be carefully handled before any further course of action. These two split up entities will be :

(1) Pakistan Telecommunication International (Pakcom International),

(2) Army Communications (Armco).

This stage will require full involvement of military experts, lawyers, resource management advisors and financial advisors. Moreover, external technical advisors and international aid agencies can also play their assist role for development structural adjustment programmes and strategic plan in the light of long term planning and development programme.

STAGE 3 : COMPETITION CREATION/TRIAL FRANCHISES

After this fragmentation, Pakistan telecommunication international (Pakcom) will need capital expansion and network infrastructure expansion. Pakcom can arrange

international joint ventures to attract the financial resources and technical assistance. This international joint venture (IJV) programme will provide an immediate capital injection, business skills and foreign experience and new employment opportunities in the industry. This arrangement of capital generation through joint venture should be earmarked for the development of telecommunication infrastructure, advanced technology and modernization of its network.

In the initial Pak Telecommunication trial period, control and ownership will be remained with the Pakistan government. The government and the regulatory body will issue licences to the three franchisers: Northcom, Southcom and Centcom for the specified period of two years in order to develop the franchise culture and an understanding of the system. Pakcom International will receive the specified fees for providing telecommunication network link time.

This "Mixed model" is a representation of American, British and Japanese telecommunications experiences and further tailored/engineered according to Pakistan's economic, cultural and political situations. This strategy may help the Pakistan Telecom to utilize combined techniques and East–West experiences which suit to Pakistan economy and telecommunication industry in order to achieve the required goals. My field studies show that Ministry of Communication and also Telecommunication's employee union realize that some of the activities better handled and run by the private sector or employees group. Two manufacturing units of telecommunication industry such as Telephone Industries of Pakistan (TIP) and Carrier Telephone Industries (CTI) can be sold through management/employee buy–out or international strategic investor. The latter can be 100% sold off, and former strategic one can be retained with at least 60% stake with Pakcom international so that it can expand its business to international level, especially

supplies of equipments to the neighbouring countries. This system should remained under state control and observation for a couple of years but it will work entirely on the commercial base and business-like approach. It will create a competitive environment in the manufacturing business as well as telecommunication services. This two year experiment and investment programme will also provide an appropriate signal for future long tem planning for deregulation and privatization programme.

STAGE 4 : DEREGULATION/PRIVATIZATION

The Pakcom International will be under supervision of new blood managers and well experience international joint venture (IJV) who would be responsible for efficiency, productivity, profits and losses of the industry. In line services, each franchise company will try its best to extend a variety of services and generate revenues to create economies of scope and to survive/flourish in the competitive market. Survival should be no problem at all because of the huge demand of the new telephone connections and other services (see Table, Chapter 7). Three new companies can initially hire the network facilities from Pakcom International.

After the initial period the government should further break down the telecommunication industry into smaller groups to create more competition in the services sector by inviting competition for at least six franchises. These new private operators can be employee groups, international companies or local public or private agencies. The licenses can be issued under terms and conditions for a specified period of time which help the franchisers to develop themselves in the competitive market and to get a reasonable rate of return from their investments. The revenues from joint venture, partnership, asset sale and franchises/line rents fees will enable government to establish and expand the network infrastructure.

No one method can fulfill the multiple objectives of Pakistan government due to the lack of political stability and absence of a coherent privatization policy. For example, sale of shares, if successful, can generate the capital for government to meet its short–term deficit requirements but the industry and customer are not getting any thing for long–term social and economic development. There are other state owned enterprises and services which can be sold to reduce the budgetary deficit including manufacturing units of the telecommunication industry.

INTERNATIONAL JOINT VENTURE WITH STRATEGIC INVESTOR(S)

The joint venture programme either in network development or manufacturing units of PTC will provide a chance to change managerial structure and culture of the industry. Foreign involvement in the telecom industry is not only a means of the capital injection and employment generation but it also transfer technical know–how, managerial, organizational and cultural knowledge to the host–country and industry (John Child and Rodrigues S. 1994). This type of international business linkage especially in the highly sophisticated telecommunication sector is extremely benefits in the developing countries. The experience also shows that initially, the coordination within international joint ventures (IJVs) is difficult because of different managerial practices, modes of business conduct and organizational cultures. Mutual interaction and adaptation is very important for the betterment of business and organizational goals. The experience of International strategic alliances (ISAs) show that American, German and Japanese prefer to introduce their business and managerial philosophies or styles. American companies stress the need for the local managers to adopt a market–oriented view of doing business with rapid introduction of western techniques. German partners tend to emphasize on the development of professional and technical competence. Japanese try to change local staff attitude and behaviour towards a strong identification with the company. This type of management style and philosophies are representation of different

cultures which increase the ability of partners and their workforces to work together, develop mutual skills and achieve the goals.

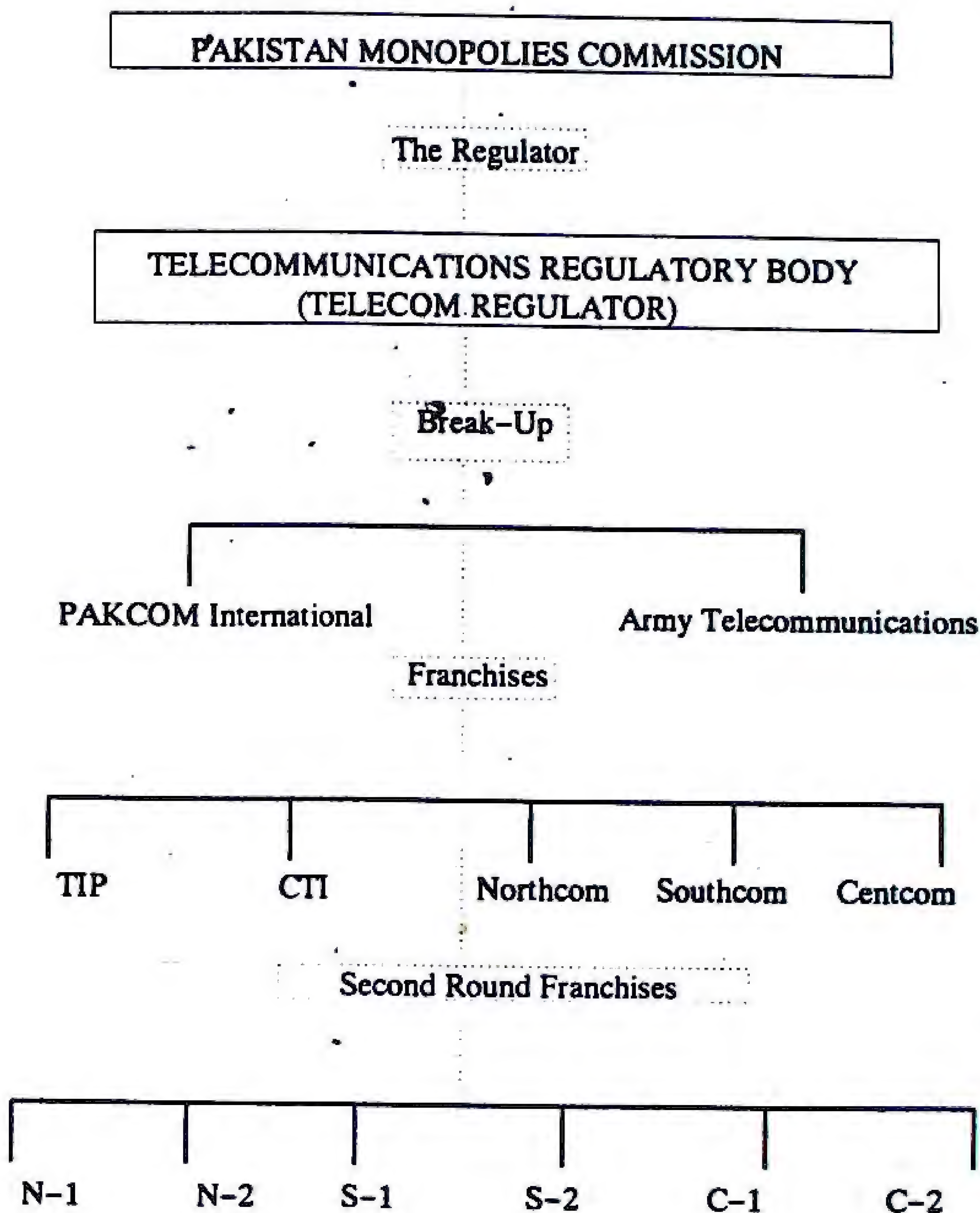
Manufacturing units of PTC can be open to these above programmes in order to get the technical know–now and managerial skills. The proposed breaking up of the Pak Telecom corporation will create the competition among the various private service provider companies or franchisers and their managers to develop the extension of communication services. Pakcom international will expand the network through BLT schemes as well. This mode will help the Pakistan government to generate the revenue and improve the productivity and efficiency through foreign experience and competition.

THE POTENTIAL FOR 'MIXED MODEL'

The government of Pakistan has been planning to privatize Pakistan Telecom for the last seven years, since the first government of Ms Benazir Bhutto in 1988. In spite of hiring different domestic and international consultancy firms and making various boards and committees for privatization of telecommunication industry, neither the present government nor previous governments actually implemented the privatization policy because of the above mentioned reasons. This model is designed to break–up industry into component parts for general public services and Pakistan army services, and for the adoption of mixed modes of privatization to help to achieve the objectives of the technological up–grading, cash inflow and experienced foreign partnership to develop the telecommunication network and create innovative markets. The new structure will also provide a chance to Pakistan telecom to become multinational company. The franchises companies will enjoy tax holidays or other subsidization in remote and unattractive areas. The industry will be more competitive and liberalized and not only be able to reduce the waiting list of customers but also expand effectively and efficiently the services to general

public at cheaper rates. This first trial experience with the help of international strategic partners and agencies will determine the further direction of the industry. The proposed structural format for the telecommunication industry can be organized as under:

STRUCTURE OF THE PROPOSED MIXED MODE MODEL



In the light of the above proposed reorganization of PTC and implementation of mixed model, the government, initially will liberalize the industry by dividing it into two entities which should be clearly defined and delimited by a Telecommuni ation Act. According to the Act some assets or activities of the industry will be transferred to Pakistan Army, then, Army Communications will arrange and run the services as per its strategic requirements. The government has to arrange an international strategic alliance (ISA) with a specified transfer of share equity for Pakcom International to develop and extend the telecommunication network and offer network services to the new franchisers to create competition within the industry.

The International Strategic Alliances (ISAs) not only provide a linkage with the international business world but also a source of advanced technological information, management techniques and latest know how (Child John and Yan Yanni 1994). Initially, this international joint venture (IJV) partnership should be established on the pattern of US-China partnerships such as "segmented control" or "devolved mutual control". The former IJV termed as segmented control, where American firm brought advanced manufacturing technologies and western management techniques and know how in return for a minority equity stake (31%). The Chinese state owned enterprise retained central control of domestic sales and purchasing while the IJV controlled modern production and technical matters with limited staff. The latter category of IJV ownership and control termed as "devolved mutual control" was launched only after a considerable period of initial cooperation and than a long term indefinite duration with 50/50 equity stake and therefore perceived the need to "progress by step function", and eventually the "take off" (Child J. and Y. Yan, 1994). Foreigners' takeovers often face resentment and volatilisation, therefore, some preventive devices could be utilized, such as 'golden shares' and 'noyaux dur'. In the light of these experiences government of Pakistan

should prefer the former category because of the strategic nature of industry. The privatization of the telecommunications industry and development of competition both require independent regulation, and involvement of different organizations such as ministry of production and industries, department of fair trading, monopolies commission and the regulatory body. The Telecom Act may needs to explain the scope and discretion of these authorities with respect to the granting of licences, modification of licences, terms and conditions of licences and licensees, price control etc. After this legal framework, the government can select an international join venture partner for Pakcom international under specified terms and condition and also can invite different interested parties/companies from home and abroad to invest in Pakistan Telecom industry under franchises modes of privatization, to improve productivity, efficiency and range of services. The management of the new company (Pakcom International) have to accept the challenge to develop and expand the network infrastructure and provide the network services to the franchisers at reasonable rates. All revenues can reinvestedtne development and extension of infrastructure of the telecommunication industry.

CONCLUDING REMARKS:

Past experience, and my personal field observations, indicate that no single mode would be appropriate for the existing circumstances for privatization of Pak Telecom due to lack of investors interest, thinness of capital market and army interest. While considering and studying all these factors, I believe, the mixed model of privatization, which is planned and proposed in this book would be an appropriate solution. The model provides a balanced public–private combination for the betterment of the government, industry and consumers. The Pak telecommunication utility is one of the biggest monopolistic industries and government should develop its privatization programme with great care in an evolutionary way, securing the support of the management and employees of the

corporation. There might be some criticism about this evolutionary approach which is divided into five phases of implementation over a substantial period of time.

However, world experience shows that the average time requirement for privatization of major state–owned telecommunication industries is from 5 to 10 years and the proposed plan is within this average time–frame.

The combination of privatization modes under different phases has been exercised in developed and developing countries eg Gambia, Jordan, Singapore, Turkey, USA and Tunisia and completed in specified period of time (World Bank 1989). The UK experience of British Telecom ran from reorganization and separation in 1981 from the post office department and privatization through three public offerings in 1984, 1991 and 1993. The Japanese Telecommunication, Nippon Telegraph and Telephone Public Corporation (NTT) was sold through the various modes of at different stages since 1985–86. The USA, AT&T was in the process of restructuring from 1977 onward, and divesture was completed in January 1984 (Philip G. and Tsoi Shao, 1988). Other examples of the telecommunication industries of Argentina, Mexico, Malaysia, New Zealand and Singapore started in mid 1980s and are still in the privatization process.

David Heald (1988) suggested that the policy reforms in the public enterprises would be a mixed policy depending on the country's circumstances. Moreover, the flotations mode of privatization would play comparatively smaller role in privatization programmes in the developing countries, because of weak capital markets, political uncertainty and lack of public interests. There are examples where governments have spent a large amounts of money on consultancy advice on utilities without getting anywhere. The British experience shows that one must be very careful while privatizing monopoly with a particular mode of ownership

transfer without introducing proper competition and deregulation. This monopoly privatization can only work well if and when competition is introduced and without it there might be serious private monopoly problem in future.

Therefore it is necessary to develop a mixed model, and gradual implementation plan that has full political and economic commitment and support. The most important thing for successful privatization is, firm commitment and a coherent implementation strategy. At the same time, international strategic investors (ISI) are desperately seeking new markets and cross-border investments. The ISI major interest is towards those countries which provide reasonably secure investment opportunities with full political commitments and Pakistan governments have to provide assurance of support within parliament and outside agencies to attract international capital, technical knowledge and managerial skills. Secondly, the restructuring of industry will divide the activities into different strategic units and this will decentralize decision-making, establish attractive incentives and delegate accountability performance to individual strategic managers. Thirdly, this model involve international strategic investors and join ventures for extension of capital and expansion of services. Fourthly it will create competition which is a key to efficiency and productivity through different service providers or franchisers.

Finally, the model will also generate capital receipts from international joint venture and franchisers which can be utilized for extension and development of network and services of industry.

CHAPTER NINE

CONCLUSIONS AND IMPLICATIONS

As examined above the privatization movement swept through the world during 1980s and became a global phenomenon. Lady Thatcher took a lead to putting the concept into practice in the 1980s. This practice set an example and *"has already prompted countries worldwide to use it as a model for their own policies"* (Moore J., 1986). From the initial privatization in Britain, France, Italy and Japan, it quickly became a dominant orthodoxy in the advanced OECD countries. The collapse of command economies in late 1980s turned the privatization into a boom in the Eastern European countries.

The United Kingdom was the pioneer in selling major state owned utilities into the private hands through stock market flotation in order to transfer the ownership public companies to millions of shareholders. The major emphasis of the privatization was to promote wider share ownership and receipts generation to meet deficit requirements. To do this, the government sold well known profit making enterprises to attract investors. The public utilities were the largest and most profitable assets that could be easily sold and produced more cash receipts than anything else (Hyman L.S., 1993). Privatization has now become a central part of both political and economical policies in developed and developing countries of the world.

The privatization movement throughout the globe is accelerating and expanding its scope towards all fields and sectors of industries and services. Around one hundred countries of the world have launched ambitious efforts to privatize in one way or

other, their public sector enterprises. International Financial Law Review April 1994 estimates that privatization programmes are expected to raise $800 billion for indebted governments worldwide by the year 2000. Since 1985 more than $328 billion has already been raised. According to Morgan Stanley, an investment bank, the sales proposed in Western Europe alone will raise $150 billion by 1998. The biggest privatization is expected in France and Italy, and with major disposals in Latin America, Eastern Europe and Asia (The Economist, August 21, 1993). Saloman Brothers forecast $55 billion in Europe, $30 billion in Latin America, $20 billion in Asia, $5 billion in USA and $10 billion in the rest of the world will be raised in equity over the period between 1993 to 1995.

The recent trend shows that the interest in privatization is growing more rapidly among the developing countries of the world. Often modelled on privatization programmes in Britain, Japan, France, USA and other industrial countries, these developed countries have common social and economic infrastructures and interests and they have some justification in copying each others socio-economic policies. Developing countries which have entirely different social, political and economic structures, needed to think carefully about the relevance of these models.

DIFFERENCES AND SIMILARITIES IN DEVELOPED AND LDCs

The developed and developing economies and cultures have different social and economic priorities which may require different routes to reform and modes of privatization. The industrial countries have already well established social and economic infrastructure and their motives are to maintain and renew the system. Whereas, developing countries are in the process of planning and development and it will take significant time to reach an equivalent level.

There is a clear gap, therefore, between developed and developing countries at the

political and economic level. There is also an obvious *"risk of treating developing countries as a homogeneous group; Thailand is dramatically different from Bangladesh, and newly industrialising countries of South East Asia bear little relationship to Sub-Saharan Africa"* (David Heald, 1988, p68). There may be more logic to copying the social, political and economic policies of the developing countries like Malaysia, Mexico and newly developed countries such as Republic of Korea, even Thailand, rather than Western industrialized countries e.g. United Kingdom, USA and France. But even this requires critical reflection, as issues of level of development, culture and politics will still create and require differences of approaches. Moreover, Western European nations are learning from their own mistakes and moving more towards liberalization, rather than simply settling for ownership transfer. The developing countries are still thinking and approaching privatization in very traditional ways, and as one commentator has noted *"it is sad to watch developing countries repeating mistakes, which have been proved disastrous elsewhere"*.

PUBLIC ENTERPRISES AND PERFORMANCE

The role of public enterprises in the developing countries has been significantly important. There has been a substantial reliance on these enterprises to achieve social and economic goals. The argument for privatization has been that at the economic level, and at the level of the firm, this has been inefficient and ineffective due to weak public enterprise performance. However, though this is widely believed, there is little systematic as opposed to anecdotal evidence to show a link between ownership per se and company performance. The linkage of ownership and performance pre and post privatization for ten UK companies during last twenty years, was examined on the basis of productivity and employment and financial ratios against change in status and competition. The researchers could not find any supportive evidence that change in ownership improved the performance of

enterprises (Dunsire D, Hartley K. and Parker D. (1991), Whitefield D. (1992)).

Even where public enterprise performance is poor, ownership is not the only or necessarily the most important matter. It may a matter of political interference, poor availability of capital and technology or excessive demands of social and political goals. It is important to identify the major causes of poor performance and inefficiency in public sector enterprises.. Furthermore common weaknesses and causes of poor performance are included: unclear multiple objectives, bureaucratic meddling, highly centralized decision making, inadequate allocation of resources, managerial ineptitude, excessive personnel costs, higher labour turnover and poor technological know how. This pervasive dissatisfaction with the performance of SOEs is at the heart of the appeal of privatization to the policy makers in the developing countries.

In Pakistan and other many developing countries the state owned enterprises are major instruments for political patronage. Staff are frequently appointed on a political basis with little industrial experience. During my study tours & **analysis,** I found high executive turnover e.g. Pakistan Telecommunication Corporation chairpersons changed 3 times during the last two years which definitely effected the performance of institution. Purchasing and pricing decisions are often dominated by social and political intervention. The boundaries of government and enterprise control are ill defined and continually shifting.

The objectives of public enterprises are often not clearly defined, and limited operational autonomy within enterprises inevitably has a negative impact on efficient internal operation. Public enterprises may be poor in achieving allocative efficiency due to a monopolistic position, and lack of threat of takeover or bankruptcy also effects productive (technical) efficiency. If markets are

competitive, the forces of competition ensure that greater allocative efficiency is achieved, and if the enterprise operates in monopolistic environment, it has little incentive to respond to market demand and is unlikely to achieve allocative efficiency whether public or private. Lack of technology and infrastructure also effect on the performance of both public and private enterprises. The evidence on technical efficiency performance does not demonstrate that public enterprises in developing countries are always outperformed by the private enterprises.

It is clearly not the case that all private enterprises are doing well in the developing countries. They also often depend on government tariff, protection, public banks and other subsidizations.

Indeed Milward suggests that the problems of political interference limited managers or autonomy, poor technical base and poor incentives characterise all sectors in developing countries. That being the case, ownership transfer alone, particularly for utilities, may not improve, and may even demage, enterprise efficiency and performance.

PRIVATIZATION AND COMPETITION

"Privatization" is often simply a political and economic slogan. The true watchwords in public sector reform are liberalization and creation of competition. Ownership transfer is a gradual process, and related most strongly to those countries who are on the way to industrial development with high level of domestic saving and developed capital markets.

As noted earlier, privatization in the developing countries is more a programme of management reforms and an evolutionary way to create competition and improve

efficiency of the enterprises. The improvement of public sector management and liberalization of capital markets are likely to bring the required efficiency by themselves, regardless of transfer of state ownership. The success of privatization is not the number of ownership transfer but the allocation of resources and creation of competition and achievement of higher rate of return from the enterprises which can reduce public sector deficits (Aylen Janathan, 1987). As the World Bank noted *"the key factor determining the efficiency of an enterprise is not whether it is publically or privately owned, but how it is managed. In theory it is possible to create the kind of incentives that will maximise efficiency under any type of ownership"* (1983, p50). To encourage improved performance it may be necessary to reform the system of incentives to enterprise management with rewards being related directly to performance.

This new strategy of improvement in internal management, often with the support of international joint ventures offers more to improve economic efficiency and performance that is the motive of privatization in the developing countries. Public sector reform along with involvement of an experienced partner, rather than pure privatization, should be the major focus of the economic reform programme in the developing countries (Cook P. and Kikpatrack C., 1988). There is no guarantee that private enterprise will definitely show the high level of efficiency and productivity in the very uncertain political and economic situation of developing countries such as Pakistan. As mentioned earlier that SOEs were formed to achieve socio-political objectives i.e. providing goods and services to a particular population, promoting industrialization and defending national interest. These additional goals were often incompatible with commercially efficient production and therefore the public sector became loss makers. Private enterprises may not care about these additional goals and may not focus on particular defined level of goods and services because their primary goals are maximization of profits.

David Heald has suggested that

> *"privatization is, thus, relevant in a number of different ways(to development). First, if privatization led to greater efficiency and/or lower financial losses, there might be a reduced call on the budget for subventions. Second, privatization of enterprises such as steel might lead to faster elimination of uneconomic capacity and, by distancing the government from the adjustment process, eliminate its legal obligation to make up losses and otherwise limit its exposure. Third, by privatizing an enterprise, the business would no longer look to government for its financing needs and, thus eliminate a claim upon the budget"* (1988, p76).

In the light of this statement, Pakistan public sector need to improve the efficiency, control losses, manage the inadequate return on investment and seek expansion of services in telecommunication and other utilities with the participation of private investment. Heald further suggested that policy mix should depend on the country's circumstances. For example, the flotations mode of privatization would play a comparatively smaller role in privatization programmes in the developing countries, because of thinness of capital market, low saving ratios and a culture of debt rather than equity. Therefore, the Pakistan government needs to work out its own approach taking account of economic, political, cultural and industrial circumstances and requirements.

NEED FOR STRATEGIC CONTINGENCY

The vogue for nationalization and state regulation in the UK and other countries post-war was not successful during 1950s and 1960s despite high hopes of its initiators. As a result a new fashion appeared in the shape of privatization in 1970s as being the only way to improve efficiency and competition by means of ownership transfer. International agencies ie World Bank and IMF also advocated this strategy but subsequently have realized that economic objectives could not be achieved

under a single mode of privatization. Therefore, these past experiences and mistakes suggest that clarity of objectives and adoption of a strategic contingency approach in designing privatization and liberalization programmes is essential. Governments should develop short term and long term objectives that should indicate what is to be accomplished, when, how and by whom. This eliminates the complexity and confusion and also help to develop the strategies to achieve the specific objectives.

THE STRATEGY AND ITS LEVELS

Strategy is a serious game that is played by the government and managers with their own and other organizations. According to Ralph Stacey

> "*Strategy is a perceived pattern in actions past or yet to come. We cannot touch a strategy or feel it – it is an interpretation we make of what has happened or what we expect to happen next. A strategy is simply a category into which we put certain patterns of action... The strategy process that deals in an analytical, rational way with the questions: How did we get here? Where do we want to go now? and How shall we get there? The important point to bear in mind is that this interpretation of what managers do or should do reflects a particular paradigm: a believe in the importance of intention, stability and regularity for the success of a system*" (1993, pp 5,7).

Strategy can be broadly defined as the match an organization or government makes between its own resources and the threats or risks and opportunities created by the external environment in which it operates. A strategy is a key link between what the organization wants to achieve (objectives) and the policies adopted to guide its activities at corporate, business and functional level. Therefore an organization can have single or many strategies to achieve the required objectives.

This strategy formulation needs proper identification of strategic options, as we did in chapter 7 and 8, and selection of a preferred strategy(ies) (Cliff Bowman and

Asch David, 1987). Privatization as ownership transfer has been a major strategic option worldwide, particularly in the UK, but proved less appropriate to achieve the wider objectives of privatization ie competition, efficiency and capital mobilization. There is a need for strategy clarification and identification of future strategies with appropriate plans to achieve long term economic objectives of privatization while encouraging different modes and learning lessons from the past experiences and mistakes. Developing countries need more effective strategic planing with a contingency approach to create efficiency, competition and link privatization to core socio-economic development.

CONTINGENCY STRATEGIES AND MIXED MODES

The development of contingency theory was a reaction against the idea that there is "one best way" to proceed. This approach is derived from empirical research that *"success was not correlated with a simple single set of factors. Instead, the effectiveness of the particular organization structure, culture, or sequence of actions in contingent upon and depend upon, a number of factors"* (R.D. Stacey, 1993, p61). The most important of these contingency factors are usually held to be: (a) environment of the country or market (b) size of the organization (c) the technology it employs (d) history and structure of the organization (e) expectation of the employees and other social groups.

This approach suggests that success will be secured when an organization secures a good match between its situation, structure and strategies. When a strategy clearly becomes unacceptable or inappropriate in an organizational environment and culture. It needs to reviewed and better tailored to the key contingencies pertaining. These alternative approaches, based on different forecasts of key variables, are known contingency strategies (James Taggart, 1991). Therefore a contingency approach is developed to suit the particular circumstances, in a

particular environment, and a particular set of objectives at a particular time. Development of this contingency approach in the privatization of Pak telecom corporation require a 'mixed mode' approach to improve efficiency, extend infrastructure and bypass weak markets and domestic investors' apathy that coused earlier strategies to fail.

PAKISTAN STATE OF ECONOMY & PRIVATIZATION

After studying and analysing the political, social and economic situation of Pakistan and its public enterprises and public utilities, particularly Pak Telecom, it still provides a depressing picture in certain sectors which are discussed in turn:

SOCIAL AND DEMOGRAPHIC ASPECTS

Pakistan is highly populated country which requires special attention to plan and manage social and demographic development. Life style and standard of living depends on the manageable population and their purchasing power. Increasing population needs better distribution of wealth and proper mobilization of resources to improve the living standard of the people. Under these circumstances the government has to improve the public systems which can have positive impact on the life of the common citizens. The social sector, for example health, education, labour and social welfare, has shown overall very little progress. In education, unfortunately, the literary rate is not more than 35%, and about 20% of the population is living below the poverty line, and the whole nation is under the heavy burden of foreign loan, where most of the aid comes from the overseas agencies most revenues from taxes etc., are being used simply to repay the loans and their interest.

In the health care side, there is one doctor for 2,008 persons and one hospital bed for 1,506 persons. The expenditures on health are only about 1% of the GNP. The

rural population has only 44% access to safe drinking water against 85% urban access to the safe water and 55% to sewerage system. The health facilities, housing condition, roads and transport systems are not up to the government's minimum standards in many areas of Pakistan. Pakistan literacy rate is about 21% female and 46% male; and the government expenditure on the education sector are 2.4% of the GNP, and it will increase to 3% during the next five year plan (Pakistan budget, 1994–95). In the decision of economic reform programmes, government has to consider the above factors as well.

THE POLITICAL ASPECT

As mentioned in chapter 3, Pakistan, unfortunately, has not succeeded in developing stable political government since its independence. History shows that the recurrence of military regimes and the tussle between revil political groups could not provide stable government to develop a long–term social–economic policy for the country. The political situation has become less stable over time, as since 1985 four general elections have been held and more than half dozen prime ministers have been changed. Three governments have been dissolved during the last two years alone. This critical situation shows, how Pakistan need a strong and stable government who can implement social–economic policies for its development and prosperity in future. The role of the government and opposition is crucial in development of the country and its way to self–reliance. They should tolerate and respect each other views and policies and try to get consensus and harmony on social and economic development programmes. The manifesto of the each party in Pakistan is nothing but socio–economic development, industrialization and self–reliance, but it requires time and co–operation with each other on the common policies and key national issues, (for example Atomic energy, Kashmir and Socio–economic reform programmes).

The broad spectrum of the political mainstream should be involved into the whole process of collective decision making. When government, opposition leaders and the media start seeking areas of consensus, it will be the first step toward to the political stability and economic development. As one senior official in a Pakistan financial institution rightly said: *"Pakistan's major problem is not economic, but political; that is where the uncertainty lies"*.

It is crucial for the politicians to treat politics as a 'serious business' rather than fighting one another at the cost of social and economic disaster. Privatization strategy, therefore, be designed to accomodate different interest and integrate them, as the proposed model does.

THE ECONOMIC ASPECT

As noted above, the socio-political system of Pakistan government shows very discouraging position. Government needs to accelerate the industrial, agricultural and thus employment growth along with the development of the physical and social infrastructure in order to improve the quality of life and standard of living in the country. Efficiency and productivity in the public sector, which is responsible for this development is not encouraging. Government representatives are claiming that Pakistan is becoming another Asian tiger while others say that we are surviving solely on foreign aid etc. This is a wrong route to impress the local and international community. Real national development needs practical comprehensive action plan for its implementation, rather than these imaginative claims.

In human resource terms, about 2.5 millions people are unemployed, the rate increasing at 5% per annum. Out of 32 million workers, 51.2% are employed by agriculture and only 12.7% employed in the manufacturing sector. However, the

growth rate of agriculture and manufacturing is around 7%, while the share of the agriculture in GDP is 26% and manufacturing is 18%. The growth rate of GDP was 6.9% and estimated 7% for the financial year 1994–95 (The Muslim, 10 June, 1994). The current social and economic policy of the government should be aimed at boosting the industrial as well as agriculture sector which is a source of raw material for various industries, to improve their growth rates and create jobs opportunities for the unemployed persons. Therefore what has been so for done, need to be thoroughly analyzed and reviewed to gain lessons and develop better integrated socio–economic strategies for the future, with full political and economic commitment and consensus.

Considering these aspects, Pakistan requires a tailored privatization strategy; a combination of methods which are best suited to the country's social, political, demographic, economic and administrative environments. Pakistan also needs transparency and stability in the privatization process, to build a confidence among the public, unions and local as well as international investors.

POLICY INSTRUMENTATION

The most important thing for successful privatization and deregulation in Pakistan is achieving "corporate consensus" within and outside parliament. This corporate consensus should be among electorates, political parties/alliances and all Pakistan public enterprises workers action committee (APSEWAC) to implement the long term socio–economic policies and to secure and build the confidence of domestic and international strategic investors.

The physical and human base of the Pakistan economy needs immediate consideration. The government needs to pay proper attention to increasing the literacy rate and developing appropriate education and training programmes for

unemployed people, coupled with the social welfare and infrastructure programmes which are the basic preconditions of liberalization and privatization policies. There are examples before us, where the government has spent a large amount of money on consultancy on privatization of utilities without implementing any strategic plans at all. The policy analysts have to consider potential obstacles and resistance seriously before designing a policy options for implementation.

The UK experience shows that privatization of the large enterprises and monopolistic utilities, such as power, telecommunication gas and water supply, required a long process of implementation. In telecommunication, an industry "Duopoly" Policy was put into effect in early 1980s and later, realising the defects of the situation, in the 1990s, the decision was made to end the duopoly policy and introduce an "Oligopoly" Policy in which new operators are issued licenses for competition. Apart from this, BT and Mercury (C&W), have other competitors in various market segments in the UK including the operators of cellular networks, personal communication networks (PCNs), telepoint, paging, cable and satellite uplink systems, information services providers and sellers of leased circuits.

As noted in chapter 5, the early experience of speedy privatization of BT and BG in the UK could not achieve the economic objectives but it did provide lessons for later stages of the programme. While considering the lessons the Pakistan government has to develop a long term framework regarding competition, protection of the potential consumers, establishment of a price regime, and development of regulatory agencies to supervise the whole privatization and deregulation process of monopolistic utilities. This institutional development will help the Pakistan utilities to improve their industrial performance, quality of services, reduction of debts and improvement of customers welfare programmes.

In the light of the above British experience one must be careful if privatizing monopolies without creating competition. As Morgan David mentioned with reference to Dick Netzer that *"There is absolutely no advantage in replacing a public monopoly with a private monopoly. What you really are after is competition"* (1992, p258). Utility privatization can only work very well if and when proper competition is introduced and this is major motive of the proposed "Mixed Model".

Past experience and my field observations indicate that no single mode of privatization would be appropriate for the existing circumstances of Pak Telecom i.e lack of investors interest, thinness of capital market and of course, the Army view point. While considering and studying all these factors, the mixed approach/model of privatization discussed in chapter 8 is most appropriate to obtain the social and economic objectives. Under the circumstances, the model provides a balanced public-private combination which would be an attractive policy for both government and for domestic and international private investors.

In sum, it is clear from the previous discussion and analysis that privatization is a dynamic and gradual process with various impacts on socio-economic development. The economists and political scientists are still arguing its strength and weakness in different sectors and countries. This debate demonstrates that privatisation is neither "good" nor "bad" economic policy, but only more and less appropriate for the nature of the industry and the circumstances of the country.

British experience shows that clarity of strategic objectives, along with learning from past, have important impacts on implementation and the learning curve of privatization. Privatization is a long term social and economic development policy

and should be designed more in rational and gradual way, rather than on a revolutionary political and ideological basis, especially in the developing countries.

As Pakistan Telecom is a strategic industry, government should develop its privatization programme with great care and in an evolutionary way, after securing consensus/support from all releveant stakeholders. Considering all these factors, the mixed model proposed as a combination of modes for the creation of competition and for securing managerial and financial investment from international strategic investor(s). Pakistan's core social and economic goals are to increase productivity and efficiency within the economy to raise standards of living for all of its population. These economic goals can only be achieved if privatization policy is properly designed, well organised and flexibly implemented. Otherwise, as Roger S. Leads (1991) quotes a Thai senior official: *"privatization is like a fire. You can cook and make good use of it or burn your house down; its all depends on how carefully you treat it!"*.

PART 4

Additonal Readings
References
Appendexs

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APPENDIX 1.1: Supplement Article by Dr M Sajid & Dr Y Xu (SBS)

COMPETITION WITHOUT PRIVATISATION: THE CHINESE PATH

Privatisation of telecommunications has become fashionable since 1984 when British Telecom was partly sold to the public. BT's success has acted as a role model for other state owned telecommunications operators. 'Few companies have remade themselves so completely as British Telecommunications plc, the state owned phone company that was privatised in 1984. Since privatisation, it (BT) has cut costs, shed its slow-moving bureaucratic systems and claimed a place as a dominant force in the worldwide telecommunications industry' (New York Times, March 1993). The success of this policy experiment may lead to the conclusion that privatisation is an inevitable component of any deregulatory process.

In China, however, privatisation is still not a realistic and acceptable way of improving management in large state owned enterprises, even when viewed in a longer term time frame. This is mainly due to political and ideological considerations. The Communist Party, the sole party in China, believes that the main difference between socialism and capitalism lies in the form of ownership; state ownership is therefore prevalent in the Chinese economy (Jiang, 01/07/1994). Although many of the state-owned enterprises run inefficiently, especially compared with township enterprises, which are jointly owned by groups of farmers and have been developed rapidly in recent years, the government has still not given up its support for state-owned enterprises. In his report to the National Congress Delegation Conference of 1995, Li Peng, Premier of the State Council, emphasised that state-owned enterprises must still retain their dominant position in the Chinese national economy (People's Daily, 02/03/1995).

Another reason, as pointed out by Wilson (1996), is the worry about social instability caused by massive unemployment resulting from privatisation. In the absence of a fully blown social security system, the government is likely to move very cautiously in transferring ownership to the hands of private sector.

To solve problems existing in state owned enterprises, Hong Hu, Vice Minister of the State Commission for Restructuring the Economy System, and a key policy-maker on state enterprise reform, said that China would continue to reform, but not to privatise, its state enterprises.

As telecommunications is regarded as a key industry in China, its privatisation, like foreign direct investment in the Chinese telecommunications network, is a sensitive and probably unrealistic policy option.

However, although Chinese telecommunications has not been privatised yet, its achievements in recent years are quite impressive. The rapidly expanding demands on telecommunications from both business and residential customers is undoubtedly one of the driving forces of change, but efforts by the government to improve enterprise management are also significant. The strategy adopted by the Chinese government is on the one hand, to improve internal management by reforming the current State-controlled telecommunications operator, the

Ministry of Posts and Telecoms (MPT) and on the other hand, to establish a competitive market by creating a rival (China Unicom). Compared with the experience of Western countries, this is a unique policy path. The questions are: Can the state owned operator achieve the advantages of privatisation by reforming itself? Can the state owned operator behave the same as a privatised one in a competitive market? Will the public benefit from competition between two state owned enterprises?

This paper will analyse the strategies and policies the Chinese government has adopted to reform telecommunications enterprises since 1978. Some of these experiences are clearly relevant to other state owned telecommunications operators, and even to some privatised operators. It seeks to ascertain whether privatisation is an exclusive way of improving enterprise management, and if privatisation is necessarily a precondition for competition.

I. GENERAL BACKGROUND OF REFORM

The Chinese economic system, established in the early 1950s, was a centralised hierarchical planning system along Stalinist Soviet lines. Plans were passed down to production units through provincial and municipal planning authorities. Directors of large factories in the priority heavy industry sectors normally had executive authority conferred upon them. Worker participation, achieved mainly through worker representative congresses chaired by directors of trade unions, mainly focused on welfare. Material incentives, in the form of piece-rate bonuses, were the traditional device used to promote productivity.

From 1957 to 1961, the government's emphasis was more on moral encouragement than material incentives, the amount of bonuses were greatly reduced. During Chairman Mao's 'Great Leap Forward' management of the economy became more ideological. At the same time, the State Council announced decisions on the administrative decentralisation of industry: central government control over telecommunications (and other industries) was handed over to provincial governments. This was consistent with one of the major phenomena of the period – a ruthless attack on the 'professionals who constitute middle administration in the national bureaucracy and middle management in industry' (Schurmann, 1968). However, Mao's target of 'catching up with America and Britain in ten years' proved unrealistic, and the national economy was seriously affected by this strategy. This was accompanied by three years continuous sharp decline in agricultural output which led to widespread famine. As a result, the government had to readjust its industrial policy by strengthening central planning and reconsolidating executive managerial authority during the period 1962 to 1965. The party was distanced from everyday operational planning. At the same time, individual material incentives for industrial workers were re-established since removal in 1961, and the responsibility of the Worker's Congress was extended from welfare to include discussion and resolution of all issues relating to workers' interests within a business enterprise. This period witnessed the rapid recovery of the economy – a successful experience later reproduced after the Cultural Revolution.

However, this 'golden period' was abruptly terminated by the Cultural Revolution of 1966 when politics and ideology became the only priority. So-called 'Revolution Committees' replaced hierarchical management in almost all levels of industry, which Mao thought would be an

effective way for workers to be directly involved in enterprise management. Piece-rate wages and bonuses were abolished again, competitive, individual and material incentives were replaced by cooperative, collective and moral incentives.

The Cultural Revolution proved to be a catastrophe for the Chinese economy. When Mao Tsedong passed away in 1976, the national economy had nearly collapsed. The Chinese government had to make strenuous efforts to reform it.

The experience of nearly thirty years since 1949 has ultimately taught the Chinese government that an economic system copied from the former Soviet Union and Maoist industrial policies are not efficient, failing to:

1. Increase personal per capita income, as opposed to national income.

2. Increase the stock of available technological knowledge, including the import of advanced technology from abroad;

3. Reduce efficiency due to a lack of motivation and commitment among managers and workers;

4. Improve allocative efficiency, namely the direction of resources to their best uses;

5. Make use of comparative advantage in foreign trade as opposed to complementary trade to fill gaps in domestic supply (Krug 1989:22).

Realisation of such inadequacies prompted the Chinese Communist Party to make a decision to undertake economic structural reform at the Third Plenum of the Eleventh Central Committee meeting, which was held in December 1978. This meeting was a milestone in the development of the Chinese economy, as it was a pivotal point for the transformation of the centralised planning economy into the so-called 'socialist market economy'.

The main idea of this reform was to create more incentives for enterprises and workers. Bonuses were restored as an effective material incentive to motivate workers and enterprises have enjoyed more and more autonomy since 1978. The main reforms, as summarised by Child (Child, 1994), are as follows:

1. Changing the distribution of property rights (in the sense of a right to use assets) away from the state through the de-collectivisation of agriculture, the deregulation of the economy (including easing of the right to establish private or collective firms) and decentralisation of much remaining regulation, and the easing of access by firms to the factors of production;

2. Shifting from hierarchical administrative regulation of economic transactions towards a system of market regulation guided by the state;

3. Strengthening the management system within producing units through an enhancement

of managerial competence and discretion;

4. Improving incentives by linking remuneration and responsibility to performance through incentive payment schemes and responsibility systems.

In order to achieve these targets, the government initiated new policies, initially just applied to a few areas and industries, and then extended nationwide by the government once proved to be successful. In the next section, the most successful policies with reference to the experience of Chinese telecommunications sector will be reviewed.

II. MAIN REFORM SCHEMES OF THE MPT

Under the guidance of the central government, different industries or ministries formulated their own reform strategies. The main areas of reform lay in the decentralisation of administrative power to lower government echelons, the development of market relations, the delegation of responsibility for performance to enterprise managers and the encouragement of incentive systems. In this section, some of the experiences adopted in the telecommunications sector (which have proved to be very successful since 1978) will be reviewed. This review reveals that some incentives created by privatisation are also partly achievable by state owned enterprises.

1. CONTRACTUAL RESPONSIBILITY SYSTEM

The so called 'Contractual Responsibility System' evolved from the experience in China's agriculture reforms, which began in 1979. Success achieved in agriculture encouraged the Chinese government to transplant this system into industry, but this was difficult given the relative complexity of the industrial system.

The government's intention was to clarify responsibility for success and failure at all levels of industrial hierarchy down to factory workers, and then decentralise the power to these levels accordingly. It commenced with a contract system, allowing direct inter–enterprise transactions and giving enterprises control over part of the surplus output above the contracted level. This was the beginning of decentralisation of government power to enterprises, while the government retained most of its authority through a planned economy structure. By 1982, this system had been applied to more than three hundred enterprises.

In 1984, the State Council decided to further extend the decision–making freedom of state owned enterprises in ten areas including production planning, product marketing, pricing of products outside the state plan, material purchasing, use of surplus funds, disposal of assets, organisation, personnel management, payment systems as well as transactions between enterprises. In the same year, the Central Committee of the Chinese Communist Party (CCCCP) published a document entitled "China's Economic Structure Reform". It specified that enterprises would become 'independent and responsible for their own profit and loss and capable of transforming and developing themselves......(acting as) legal persons with certain rights and duties'. Their directors have conferred upon them full responsibility for their performance under a unified management system. These responsibilities include:

1. Determining the enterprise's operation and organisation, including more flexible and diversified forms;

2. Planning its production, supply and marketing in tune with market mechanisms;

3. Setting prices within limits prescribed by the state;

4. Retaining certain budget funds;

5. Deciding on recruitment, personnel and reward policies.

In this so-called 'Director Responsibility System', enterprises, especially directors, have enjoyed higher autonomy than previously. Directors' incentives were also stimulated, as their promotion and succession were linked to their performance and achievements. At the same time, of course, they were also subjected to higher pressures, both from the authorities who supervise their performance and from employees in the enterprise who depend on their commitment. These incentives motivated directors to work harder, transforming erstwhile party or government agents into entrepreneurs, who could run their enterprises independently with modern management techniques, especially after government organised training. As a result, business efficiency has been greatly enhanced.

In order to formalise the Director Responsibility System, the Contracted Management Responsibility System was established in 1986 in many state owned enterprises. Although it was applied in different industries, there are several common features involved. They include:

(1) The governance of relations between enterprise decision makers and supervisory agency by some form of explicit contract;

(2) The participation of an enterprise director into a contract on behalf of an enterprise whilst assuming personal responsibility,

(3) Some assumption of risk by the contractor, along with variability in his/her rewards, both linked to the performance of the enterprise;

(4) contract terms that extend over several years.

The MPT started to employ the Contractual Responsibility System quite early. From 1980, all the provincial PTAs signed agreements with MPT according to the principle of 'double contracting and single link'. The first contract means the enterprise is obliged to hand over an agreed amount of annual profit and tax (although profits were not accurately estimated, a problem highlighted later on) whilst retaining a proportion of any surplus it achieved above the contracted level. The second contract ensures the enterprise must guarantee to invest in order to increase asset values and develop technology by an agreed amount during the period of the contract. The single link means that up to 70 percent of the increase in overall profit can be used to fund salary increases, linking individual interests with their performance.

In 1982, the MPT adopted a 'Three-Year-Term Profit Rolling Contract System'. This system defines an annual growth rate of overall profit within three years, each enterprise's performance being assessed according to the contract every year. This overcame the disadvantages of short term contracts as some directors adopted a short term approach and management lacked long-term development strategies.

Since late 1985, MPT, along with other industries in China, utilised a Contractual Management Responsibility System. Directors of the provincial PTAs sign contracts with the MPT every year. After negotiation, objectives such as traffic, revenue, service quality and efficiency targets are contractually defined which also quantifies the reward and penalty measures. In order to prevent any short term behaviour, and give incentives to directors, four-year appointments are also signed. When the appointment period expires, the performance of the director is reviewed. Based upon the result of this review, the authorities decide if the director should be re-appointed, promoted or dismissed.

In October 1986, the contracting principle was extended to internal management of enterprises. It ranges from employment to production. It abolished life-tenure or the 'iron rice bowl' for newly recruited employees, and made any contract renewal conditional upon their performance and the needs of their enterprises. At the same time, every employee signed a contract with the enterprise specifying the required quality and quantity of a product, the reward and penalty for their performance, their responsibility in the production as well as the corresponding rights and powers granted. This made every employee clear about their responsibilities, rights and interests giving them extra incentives to work hard.

The system of responsibility has been improved, and is still used nowadays following its adoption in the early 1980s. The fact that it has been utilised for such a long time itself evidences its success. As a result, the production efficiency has been improved greatly. The MPT, for example, enjoyed 37 per cent increase in overall labour productivity in 1992 compared with 1991, (People's Posts and Telecommunications, 14/01/93), a 51.9 per cent increase in 1993 compared with 1992.

2. BUSINESS ACCOUNTING SYSTEM OF THE MPT

The Contractual Responsibility System has proved to be a very successful management scheme. However, there exists a problem of management accountability, that is, how to quantify the results clearly and accurately. If this issue is ill defined, then the contract cannot be accurately specified, and the directors' achievements cannot be fairly assessed, making the contract worthless.

In other industries, a general business accounting system is applicable. For telecommunications, however, a special accounting system is required due to its unique 'production' characteristics.

The most evident and discrete characteristic of telecommunications is that the whole process of communication, especially long distance communication, is a relay process, conducted across the network, requiring the joint contributions of at least two parties. A complete long

distance telecommunications process is described by following diagram (Fig 1):



Fig 1 Long-Distance Telecommunications Process

The originating customer accesses his local telecommunications carrier and starts the process of communication. Unless the two customer terminals are directly linked, messages are transmitted from the first carrier, via a series of 'transit' carriers to their recipient.

It is obvious that each carrier 'enterprise' provides a critical link in this process as communications are blocked if any one link is out of order. It is therefore impossible to complete a communication without cooperation between these telecommunication enterprises. However, the transmitting customer is only charged by the first carrier, while the relay, by the transit and delivery carriers, is not directly paid. How to allocate the costs in this process, and how to allocate the total revenue in general, is a major problem in any telecommunications accounting methodology. Otherwise, any incentive by the transit/delivery carriers is frustrated by their contribution remaining uncompensated.

In the early 1950s, telecommunications enterprises in China used to adopt a 'treasury system'. That is, enterprises handed over all their income to provincial PTAs every day or every week. The enterprise would request expenses from the provincial PTA for authorization, and receive the appropriation retrospectively. In this system, enterprise did not care about income as it in no way benefitted them. They were unconcerned about cost management, since expenses were simply re-claimed from PTAs and the MPT. The direct result of this system is that enterprises were managed inefficiently. Business performance and operational efficiency could not be measured accurately as profits or losses did not require to be calculated. In addition, directors of enterprises were not able to take responsibility for the performance of their business operation.

In the early 1960s, the MPT implemented the so-called 'appropriation according to budget'

system. With this system, each enterprise proposed their budget to provincial PTAs before the start of a new fiscal year. After the authorization, the PTA would issue the 'appropriation quota memorandum (command)' to enterpris.s every month or season. The enterprise kept part of the income according to the memorandum, and handed over the surplus to the provincial PTA. Compared with the 'treasury system', this system encouraged improvements in cost management, as the enterprise had to control its costs to meet the authorised budget, rather than claim them all back afterwards as it did under the 'treasury system'. However, it was still a bureaucratic system typical of a planned economy. Business performance and operational efficiency were still not assessed quantitatively and directors were only responsible for budget making and execution rather than actual profit and loss.

From November 1969 to the early 1980s, the MPT implemented the so-called 'difference management system', where the difference refers to that between income and expenditure. According to this system, the enterprise agreed to hand-over the income-expenditure difference every year, and any surpluses were to be shared between the provincial PTA and the enterprise. Compared with those two former systems, this system placed pressure on the enterprise and its directors, as they had to be concerned about the result of their operation in order to achieve the agreed difference. Their incentives were stimulated at the same time, as their enterprise could benefit from their surplus from the difference. Although these advantages render this system more satisfactory, it is still imperfect for the following reasons.

First, as mentioned earlier, a key characteristic of long distance telecommunications is that it is a relay process conducted 'along' the network, but the original customer pays the initial carrier. Carriers involved in call relay, transit, and delivery are not directly paid. In this sense, those enterprise revenues do not reflect their performance or contribution.

Secondly, it is dangerous to encourage the enterprise to focus on call-generation income only, rather than call transit and termination services. This may lead to a lack of coordination within the network, to the detriment of telecommunications quality and revenue.

Thirdly, the cost and expense of operations vary according to the geographic location of the enterprise even for identical services. For example, some places – a poor economy – may have only limited demand for a telecommunications service. Lack of economies of scale will result in high operational costs, a factor which this system dose not take into account.

Fourthly, for telecommunications, the difference between income and expenditure within one enterprise does not actually equate to overall profit. Only the total income-expenditure difference among the whole network is equal to overall profit. If profit cannot be calculated, then corresponding business and operation indicators such as labour efficiency, ratio of profit to production output etc cannot be calculated, and results cannot be clearly measured.

Fifthly, there is no strong foundation for defining the contractual difference. There are contradictions between the interests of PTAs and local telecommunications providers.

Due to the above considerations, the 'difference management system' was still a bureaucratic system with many disadvantages. Business accounts could still not be clearly measured, with

few incentives. Moreover, enterprises, by encouraging high income only, did not encourage cooperation among different service providers, and experience shows it was not a successful system.

Realising these disadvantages, the MPT started to implement a business accounting system. This system was the subject of an experiment within Hubei and another two provinces during 1983–84. Very positive results were achieved, and in consequence this system was adopted nationwide in 1985.

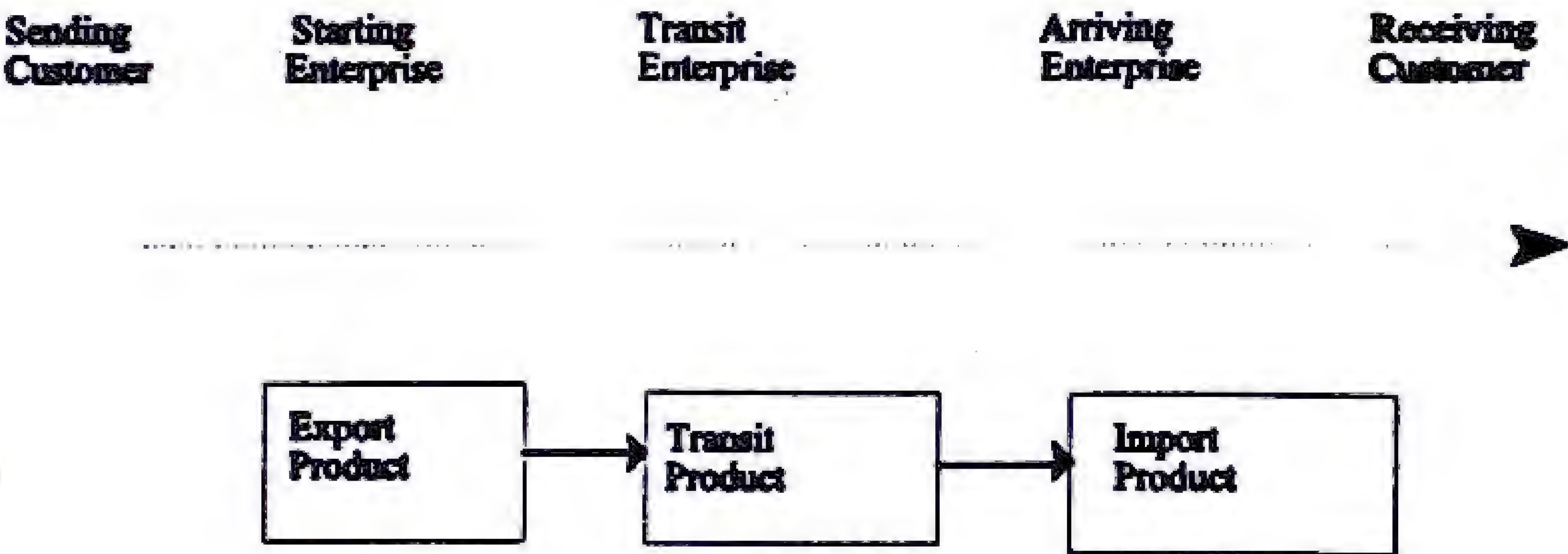


Fig 2 Classification of Telecommunications Products

The major breakthrough of this system was that it defined how to calculate an individual provider's own income, the so-called 'Enterprise Own Revenue' (EOR). It is actually a method of re-allocating the whole network's income, especially long distance service revenue, according to an individual enterprise's contribution towards the network operation. If a local telephone provider's revenue can be calculated accurately, then the profit or loss can also be analyzed within relevant parameters. Based upon this, the directors' achievement can be assessed clearly, and responsibility, reward and penalty can be more clearly defined in their contracts. Only by using this methodology could the Contractual Responsibility System become a practical and feasible management scheme for telecommunications.In order to calculate the EOR, the MPT classified the nature of the call transferred through the originating provider, transit enterprise, and call terminator as "export product", "transit product" and "import product" respectively (Fig 2). For each product, there is a fixed price which was determined by cost allocations conducted by the MPT. The price is fixed for about ten years and is then

renewed by MPT. Table 1 shows part of the latest price catalogue released in 1991 (Guo & Xu, 1992). All the long distance traffics in telecommunications, including 'export', 'transit' and 'import', is recorded by the enterprise. Then the sum of the traffic of each 'product' multiplied by its corresponding price equals the total long distance telecommunication service revenue of that enterprise. Then using this method, the contribution of each enterprise to each procedure can be calculated and charged. Enterprises increased their attention to 'transit' and 'import' services since they also obtained revenues from them as well. In this way, cooperation among individual enterprises is encouraged, and both the volume of traffic and quality of service has improved greatly.

Table 1: Business Accounting Prices for Telecommunications (1991)

Name of Product	Accounting Unit	Unit Price	Name of Product	Accounting Unit	Unit Price
Export Telegraph	unit	0.5607	Export Long-Distance Telephone	unit	1.7345
Import Telegraph	unit	0.5455	Import Long-Distance Telephone	unit	2.1188
Transit Telegraph	unit	0.2267	Transit Long-Distance telephone	unit	2.4614
Export Faxmile	unit	6.8648	Long Distance Cable	Km	15041.38
Import Faxmile	unit	89.7907	Satellite Television Channel	hour	538.366
Export Telex	time	1.3254	Satellite Telephone Channel	circuit/day	45.2288
Import Telex	time	0.8423	Satellite Telegraph Channel	circuit/day	4.7689
Transit Telex	unit	0.4054	Export Teleconference	time	14.8075
Radio Transmission	KW*Hour	10.1133	Import Teleconference	time	27.1951
Radio Receiving	KW*Hour	12.4663	Transit teleconference	time	27.4445

proposed in 1985, it had just one set of prices instead of nine, which simplified the problem of deciding a price. In order to re-allocate the revenue in a fair way, the MPT proposed the so-called 'Cost Variance Coefficient'. Seven factors were chosen from more than twenty criteria as the most relevanting in affecting the cost of telecommunications services in an area (Xu & Guo, 1992). The parameters help objectively to describe the different conditions in each area. This is achieved through multi-factor regression using the seven factors including the ratio of mountain areas, the number of days without frost within a year, the ratio of residents in the city and town to all residents in that region, the average consumption of telecommunications per square kilometre, the average GNP per capita, the density of railways and roads, and the average wage per employee. After the regression, every area is allocated a Cost Variance Coefficient (CVC). When CVC is used to set the standard price, a special price for an individual area can be calculated. Finally, the above formula can be used to calculate the Enterprise Own Revenue.

Since the application of the business accounting system in 1985, the management of telecommunications has improved dramatically. According to Liu Wangjin, Deputy Director of the Department of Finance in the MPT, the business accounting system makes 'the directors and employees feel that they are owners of the enterprise, and begin to raise concerns about the performance of the business operation. Conscious of improving management efficiency, service quality has been enhanced. The production cost has been effectively controlled and economic benefit to the enterprise has improved greatly' (Guo & Xu, 1992).

3. MATERIAL INCENTIVES

Before commencement of the reforms in China, people's expectations were linked to the so-called 'iron rice bowl', which means that everybody was effectively guaranteed a job for life. The most obvious disadvantage of this system is that high productivity is not encouraged, as people's payment is not linked with their performance. The government used to motivate staff by moral encouragement such as organising socialist work competitions. However, after the cultural revolution, there was a 'crisis of belief' among the Chinese people. Management schemes with political overtones were no longer effective, and money became the first priority for many. In this situation, material incentives were again used to motivate employees, mainly in the form of bonuses. 'In practice, a relatively egalitarian distribution of bonuses and other incentive payments continues to prevail, especially in the state sector. More progress appears to have been made towards linking payment to a person's level of responsibility, education and training, and to the profit performance of the enterprises' (Child, 1994). The amount of bonus that the enterprise was allowed to distribute and that to which an individual was entitled were clearly specified in the contract.

From 1985, the MPT began its wage reform. The purpose was to link the employees' incomes to the performance and achievements of their telecommunications enterprise, and hence provide them with an incentive for offering better customer service. In order to stimulate cooperation throughout the network, the growth rate of wages was initially only linked with traffic growth rate. The former was determined by a formula based on 50 per cent of the provincial traffic growth rate and 50 percent from the national traffic growth rate. This system was good for promoting cooperation, but incentives to increase revenue (eagerly desired by the

MPT for its further investment) had still not been effectively stimulated. In order to solve this problem, the MPT altered the formula to include revenue as an additional factor in 1993. Salary growth rate is now determined by a formula using 40 per cent of the national traffic growth rate, 30 percent of the regional traffic growth rate, and 30 percent of the regional revenue growth rate. This formula not only encourages enterprises to cooperate with operators in other regions for long distance services by considering growth of all kinds of traffic (originating, transit and termination), it also encourages them to increase their own revenue as they can benefit from this growth as well. Experience has shown that this system works well, and employee income has increased steadily.

4. FLEXIBLE FINANCING POLICY

Blackman, (1992) argues that it may be true that the considerable cost of telecommunications networks cannot be financed solely from most countries' public sector funds. However, this does not necessarily mean that private investment has a major role to play in all countries. China, for example, is still a developing country. With its GNP per capita still below the world average level (at $485.00 in 1993, it is ranked 103 out of 132 countries in the world, People's Daily, 31/08/1995), it is difficult to imagine how the private sector could afford to finance the entire cost itself of an advanced telecommunications system, at least within the near future. Like most other countries, it is also very difficult for central government to finance the system by itself.

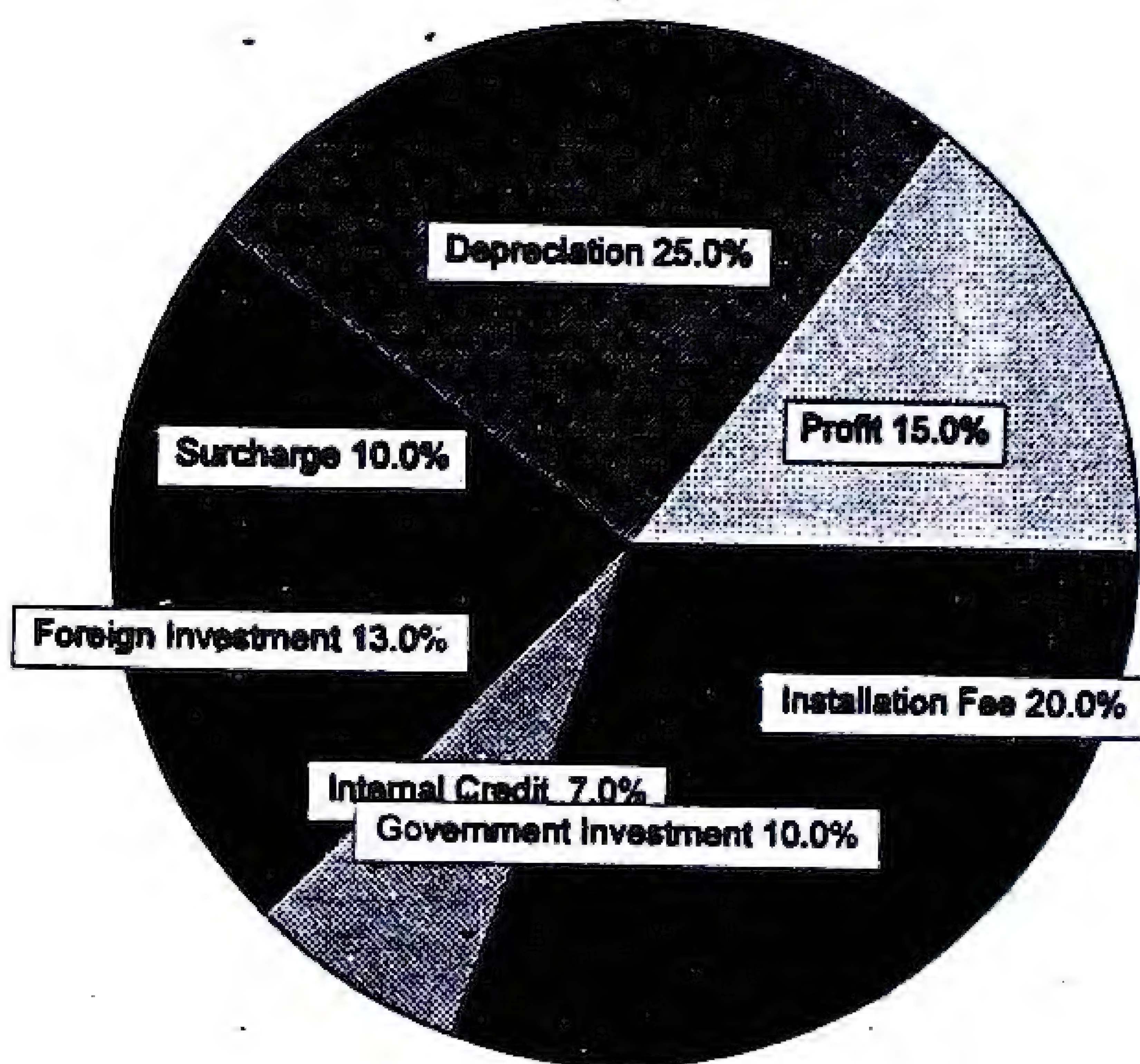


Fig 3 Structure of MPT's Financial Resources in 1994

Realising this situation the government issued an edict to the MPT in 1984 which encouraged it to adopt a policy of financial diversification, with investment from central government, local government, corporations, and a proportion of private sector funding. Foreign loans, rather than foreign direct investment, have also been used as one of the main financial resources. The above chart (Fig. 3, based upon an interview) shows the structure of MPT's financial resources in 1994. At the same time, MPT has benefitted from a variety of concessions from central government. This includes the policy of the 'three 90%s' and permission to collect installation fees from subscribers.

The three 90%s policy, means

(1) 90% of profit is retained by the local provider (in other words, the tax rate is 10%, much lower than 55% tax rate for other industries);
(2) 90% of foreign exchange (hard currency) earnings are to be retained by the enterprise;
(3) 90% of the central government's investment is considered as un-repayable loans (Wu & Zhang, p201, 1992).

This means that local telecommunications enterprises are allowed to collect installation fees from customers applying to subscribe to the public telephone network. The amount of the fee is subject to the degree of demand. Compared to the country's per capita income, China's installation charge is perhaps the highest in the world. In Beijing, for example, the installation fee is 5,000 Yuan (about £420). The installation fee can be thought of as pure-profit, as it does not involve much expense. Local revenue is therefore dependent on the installation fee. In Shanghai during the period 1980 to 1991, for instance, nearly a quarter of network investment finance came from installation fees (Ding, 1994).

So far, we have provided an overview of four innovative management schemes adopted in Chinese telecommunications: that is, the contractual responsibility system, the revenue re-allocation system, the material incentive scheme and flexible financing policy. Based upon this, we have conducted an analysis of how these schemes work in improving telecommunications enterprise management and promoting telecommunications development. Labour productivity, revenue growth rate, average income per capita and other indicators have demonstrated that these schemes are effective. Since reforms started in the late 1970's MPT is said to have successfully overseen the most rapidly developing sector in China (Zhao & Zhu, People's Posts and Telecommunications, 16/02/93). It is not an exaggeration to argue that these schemes have, at least to some extent, achieved similar results to privatisation in improving internal enterprise management and financing necessary investment.

The following diagram outlines the government's achievements using these methods.

Income from local network services is retained by the local enterprise and is not re-allocated.

As finance is critical to further development of advanced telecommunications, any increase in income is important: the MPT therefore encouraged the local enterprises to increase their income by allowing them to retain an increased proportion (currently 40%) of their income compared with previous years.

Then, the total Enterprise Own Revenue (EOR) of an enterprise is as follows:

Total EOR = Traffic of Export Products * Export Products Prices + Traffic of Transit Products * Transit Products Prices + Traffic of Import Products * Import Products Prices + All Income from Local Network Services + (Income of this Year – Income of Last Year) * Retaining Rate

It can be seen that this method has the following advantages:

(1) For the first time it offers a way of measuring the complete result of each entity's operation allowing profit or loss to be calculated. It offers a quantitative method to management and thus makes the Contractual Responsibility System feasible in the telecommunications sector;

(2) By remunerating them for their transit and terminating contributions, it encourages individual enterprises to cooperate in the process of telecommunications, which improves network co-operation and improves service quality, and leads to an increase in the traffic over the whole network;

(3) It provides an incentive for telecoms enterprises to increase their income, which facilitates recovery of previous large investments and allows the collection of sufficient finance for further investment;

(4) It creates incentives for enterprises to develop themselves, as they can benefit both from their contribution to the network traffic and their share of increased income.

As mentioned earlier, the geographic location of telecommunications providers impacts upon the cost of their operation. In order to solve this problem and re-distribute income in an equitable way, the 1985 scheme divided China's 30 provinces into nine groups according to their local conditions, each group having a set of corresponding accounting prices. For provinces in adverse positions, the price for accounting purposes is correspondingly higher, which means they are compensated appropriately for their service compared with provinces in other more favourable areas. This created many disputes among these provinces as to who should belong to a group with low accounting prices rather than in a group with higher prices. At the same time, calculating nine sets of accounting prices was also complicated due to the considerable work in analyzing the cost allocations (The precise allocation of cost is a generic problem in all telecommunications systems).

In 1988, the MPT again re-adjusted its business accounting system. Similar to the one

	Decentralisation	Market Origination	Delegation of Responsibility	Create Incentives
Contractual Responsibility system	*	*	*	*
Business Accounting System	*	*		*
Material Incentives			*	*
Flexible Financing Policy	*	*		

Fig 4 Illustration of Purpose and Achievements of Telecommunications reform in China

III. COMPARISON OF INTERNAL REFORM WITH PRIVATISATION

Summarising the objectives of privatisation Kok (1992) noted the following points: First, financial objectives can reduce government deficit and create stable mechanisms to raise investment funds from the private sector. Secondly, political objectives are designed to encourage popular capitalism via widespread shareholding and special arrangements for 'small' shareholders demonstrating international openness and a market economy orientation. Thirdly, business objectives are aimed at transferring a state monopoly into a competitive business, 'which means not only creating internal shock within the company but also opening the business to external scrutiny' (Kok, 1992) .

The following analysis illustrates that these objectives can, to a large extent, be achieved without privatisation, but instead, through reform of the contemporary Chinese telecommunications provisioning paradigm.

FINANCIAL OBJECTIVES:

In China, the government has traditionally been the sole investor in the telecommunications sector. However, it has become more and more difficult for it solely to sponsor this sector as telecommunications is such a high-tech, capital intensive industry. By applying a flexible financing policy, capital injections can be sourced from all available sectors, including foreign sources, and the government is able to divest itself of this heavy burden. As shown in Fig 3 only ten percent of the total investment of MPT came from government in 1994. In this sense, reform of Chinese telecommunications, like privatisation elsewhere, has achieved its financial objectives. The difference is that it has not just raise the finance from the private sector itself, but has also helped stimulate other available resources.

POLITICAL OBJECTIVES

For ideological reasons, the goal of popular capitalism cannot be a declared objective of Chinese telecommunications reform. However, telecommunications reforms, outlined below, are clearly linked to China's political ambitions

First, by completely opening the telecommunications equipment market and encouraging indirect foreign investment, China has shown its willingness to open the door to the outsiders – a policy unthinkable in the not too distant past, although foreign corporations are at present still kept at arm's length from any direct ownership of the telecommunications system.

Secondly, by decentralising power to local enterprises, clarifying the responsibilities of their directors through the contractual responsibility system and linking benefits to their performance, enterprise members are effectively encouraged to exhibit more market-orientated behaviour. This perhaps represents the first green shoots of a socialist market economy with Chinese characteristics.

In this sense, it can be said that key political objectives demonstrating international openness and encouraging a market economy orientation, are consistent with contemporary telecommunications reforms.

BUSINESS OBJECTIVES

It is hard to imagine an unreformed telecommunications monopoly – bureaucratic, inefficient and poorly equipped and dependent on huge government subsidies – that can compete effectively with any other newly created rivals. In this sense, it is an achievement of the reforms that Chinese telecommunications are ready for competition. For example, without a state-of-the-art telecommunications network with ninety-nine per cent switching, digitalized equipment, interconnection would be impossible, and therefore any degree of competition would be hard for new entrants. China Unicom's appearance has added further to the pressures for internal MPT reforms and creation of a competitive telecommunications market.

In conclusion, most of the objectives of privatisation have been achieved by recent reforms in China's telecommunications sector. The question now is: can a reformed state monopoly operator react to competition as readily as a privatised operator, and will the public benefit from such competition.

IV. COMPETITION WITHOUT PRIVATISATION

The establishment of China Unicom has increasingly made the MPT subject to higher competitive pressure. MPT has had to expand its emphasis from focusing on merely improving its internal management to strengthening its ability to compete with China Unicom. In fact, MPT has taken several steps to respond to the competitive pressure from its new rival, and an internal development strategy has been formulated. The main points of this strategy are:

1. To gain market share in anticipation of demand with 'pre-emptive' investment. That is MPT will invest in new services even though current market demand does not yet

justify them. In this way, the MPT expects to perpetuate its traditional dominance in the future competitive market-place.

2. To co-operate more closely with the PLA (military) and the Ministry of Broadcasting, Film and Television. Both have their own private networks and are large consumers of telecommunications. So far, these two sectors have not joined with China Unicom. An effective relationship with these two sectors would undoubtedly strengthen MPT's ability to compete with China Unicom, and at the same time help retain its current market. However, whether these two ministries are keen on this kind of cooperation and how long such a relationship can last remains an open question.

3. To create infrastructure jointly and collaborate with other partners. This opens a door for investors, both to Chinese corporations and to their foreign counterparts. However, details of this policy have not been published yet, and how far this policy can go is similarly unclear. According to Ure (1994), Director of Hong Kong University's Telecommunications Research Project, the MPT has begun to 'tinker' with the concept of new foreign investment mechanisms to meet its annual funding shortfall which is estimated at between \$3 billion and \$7 billion, depending on foreign exchange fluctuations and line costs. Ingelbrecht (1994) has noted that the MPT has recently thrown its weight behind equity-linked lease agreements. According to these agreements, foreign operators lease equipment to Chinese PTTs for a fixed rate of return, with the option to convert their agreements to equity stakes when foreign ownership restrictions are relaxed. This arrangement gives them a share of the profits and the right to conduct some degree of management control. According to Ingelbrecht, Hong Kong Telecom, Thailand's TelecomAsia PCL and Canada's BCE Inc. are said to have signed such agreements with the MPT.

The MPT has also consistently tried to create entry barriers for China Unicom. These include: a ban on undertaking projects from China Unicom by its affiliated design institute, stemming a flow of talent that otherwise threatened MPT with a staff exodus to China Unicom, adopting a hostile attitude to the establishment of China Unicom's local branches, an unwillingness to allocate frequency spectrum to China Unicom, dominating number resources and a starting a telecommunications price squeeze.

At the same time, MPT has tried very hard to exploit existing government concessions before Unicom forces their removal. For example, the Beijing Telecommunications Authority (BTA) tried to apply to raise telephone installation fees from 5,000 Yuan to 7,000 Yuan in advance of China Unicom 's entry while BTA retained its captive customer base before competition started. However, their application was turned down by the State Price Administrative Bureau.

The available evidence suggests that MPT has been forced to react to the appearance of China Unicom in a swift and strategic way. In this, it is adopting the behavioural characteristics much in evidence in newly privatised (or about to be privatised) PTO incumbent operators in a variety of other countries.

It is significant in fact that although China Unicom was only established in mid-1994, MPT customers had already benefited from the competition between the two operators. A clear example occurred when the BTA lowered its analogue mobile cellular handset sales price in April 1995 for the third time since the previous May. Price reduction ranged from several hundred to 2500 Yuan. Currently (1996) the price of all analogue cellular handsets are below 10,000 Yuan, which contrasts sharply with the price of 20,000 – 25,000 Yuan (£1,666–2,083) eighteen months earlier. BTA also lowered service charges from 0.50 Yuan/minute to 0.40 Yuan/minute. Basic monthly fees were cut three fold from 150 Yuan to 50 Yuan. (China Telecom Newsletter, May 1995). This frequent price reduction was precipitated by the opening of China Unicom's GSM network in Beijing in July 1995.

Additionally MPT has begun to take customer's interests more seriously. Several working teams have been sent out from Beijing to monitor service quality and respond to customer complaints, marking a major shift in MPT policy towards customer care, (China Telecom Newsletter, January, 1995).

Such evidence suggests that the public benefits flowing from competition are not exclusively dependent on privatisation but can emerge from an enlightened policy of managed competition coupled with effective internal structural reforms.

V. SUMMARY

First, telecommunications reform in China has successfully created incentives for telecommunications enterprises; privatisation is not the only way to improve telecommunications enterprise management. According to the analysis in section III, most objectives of telecommunications privatisation can, to some extent, be achieved by reforming the internal structures and processes of state-owned Chinese telecommunications.

Secondly, both reform and privatisation are contingently related to national culture and environment. Privatisation is not acceptable in contemporary China for obvious ideological reasons. Reform schemes reviewed in this paper are mainly suitable for telecommunications systems evolving from a highly centralised system towards a market orientated economic system, where the government still maintains overwhelming powers of intervention. In these circumstances government will ensure that only a restrained model of liberalisation will be adopted. Privatisation cannot inevitably act as a universal 'one best way' policy exemplar for all such societies.

Thirdly, as privatisation is not the only model to improve enterprise management, it should not necessarily be seen as a precondition for competition. Experience in Korea, for example, has shown that the state owned enterprise could achieve the same result from competition (Kim, 1993). What has happened in China so far is that the state owned operator has behaved similarly to privatised enterprise in a competitive market, and the public has already benefited from this competition.

In brief, for countries where privatisation is not available as a viable policy option, telecommunications competition is still feasible, provided telecommunications enterprises are reformed along the lines of a market driven operator. Privatisation and internal reforms alike can create incentives for development, while competition can act as a surrogate for full blown privatisation. Nevertheless both privatisation and limited liberalisation are not so much the end, but the means. The final purpose of the government is to promote the development of telecommunications and protect the interests of the public. In this regard the Chinese example demonstrates that a more limited approach to change and technological development may be as effective as a more 'heroic' privatisation scheme. In its wisdom, the Chinese elite have devised a unique solution to the age old problem of better serving public needs whilst simultaneously retaining a considerable degree of influence in this key policy sector. The long march to Chinese telecommunications reform is perhaps best viewed as a journey of a thousand small but significant steps!

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APPENDIX (2.1)

WORLD BANK SUPPORTED OPERATIONS IN DEVELOPING COUNTRIES

Countries and Regions	No.of operations	Lending modes	No of operations
Sub-S.Africa	95	SALs	71
L. America & Car	40	SECALs	43
Europe	19	TALs	31
Asia	21	PERLs	18
Middle East	7	" & other	19

Source: Sunita, Nellis and Mary Shirley's 1992

The world bank provids loans, for structural adjustment loans (SALs), sectoral adjustment loans (SECALs), technical assistance loans (TALs) and public enterprises reform loans (PERLs). During the last decade the bank has given these loans to the above developing countries of the world to develope and accelerate their privatization and deregulation programmes.

APPENDIX (3.2)

(a) MANAGEMENT OF PRIVATISED MUSLIM COMMERCIAL BANK (MCB)

(1) Mr. Muhammad Mensha, Chairman of MCB
(2) Mr. S.M. Munir, Vice Chairman of MCB
(3) Mr. Muhammad Hussain Lawai, The President of MBC
(4) And other members of the board of directors.

(b) MANAGEMENT GROUP OF ALLIED BANK LIMITED

(1) Mr. K. Latif, chairman of Allied management group
(2) Mr. Mushtaq Taj, the president of management group
(3) Mr. Fakher Rashidy, Senior Vice President & Director
(4) Mr. Shoukat Kazmi, the s.v.p. of the management group
(5) Mr. Javed Hussian, SVP and Secretary of the group
(6) Other members and board of directors.

APPENDIX (4.3)

UK GOVERNMENT'S POLICIES OF THE LAST HALF CENTURY

S/No	RULING PARTY	PERIODS	THE GOVT. POLICIES
1	Alliance of 3	1940–45	Industrial centeralization
2	Conservative	May–July	Supported the war efforts
3	Labour	1945–50	Major Nationalization
4	Conservative	1950–55	Overall Denationalization
5	Conservative	1955–59	Denationalization
6	Conservative	1959–64	" " Free Competitive Market
7	Labour	1964–66	Public mgt. policy
8	Labour	1966–70	Extension of PEs
9	Conservative	1970–74	Against to Nationalization
10	Labour	1974–79	Extended to SOEs
11	Conservative	1979–83	Denationalization
12	Conservative	1983–87	Deregulation/libraliz
13	Conservative	1987–92	Utility privatization
14	Conservative	1992–94	Further extension of the privatization

Source: Compiled from Fraser & Wilson(1988)

APPENDIX (7.4)

SALES AND PROFIT TRENDS ANALYSIS

Years	Sale/Growth	Sale Trend	Profit	Gen.Trend
1992	16780	21%	11597	25%
1991	13894	40%	9297	63%
1990	9954	19%	5712	12%
1989	8374	28%	5092	17%
1988	6549	19%	4346	19%
1987	5514	19%	3666	26%
1986	4560	19%	2920	22%

Source: Pak Telecom 1992–1993.

APPENDIX (7.5a)

PTC COMMON SIZE STATEMENTS: TIME SERIES ANALYSIS

(Rs in millions)	1990	1989
Operating Revenue	9954 100/100	8374 100/100
Expenses: Opert/Admin	1946 (20%)	1456 (17%)
Maintenance	779 (8%)	678 (8%)
Depreciation	1517 (15%)	1148 (14%)
Total Operating Expense	4242 (43%)	3282 (39%)
Operating Income	5712 (57%)	5092 (61%)
Interest Charges	300 (3%)	300 (4%)
Retain Earning	5412 (54%)	4792 (57%)

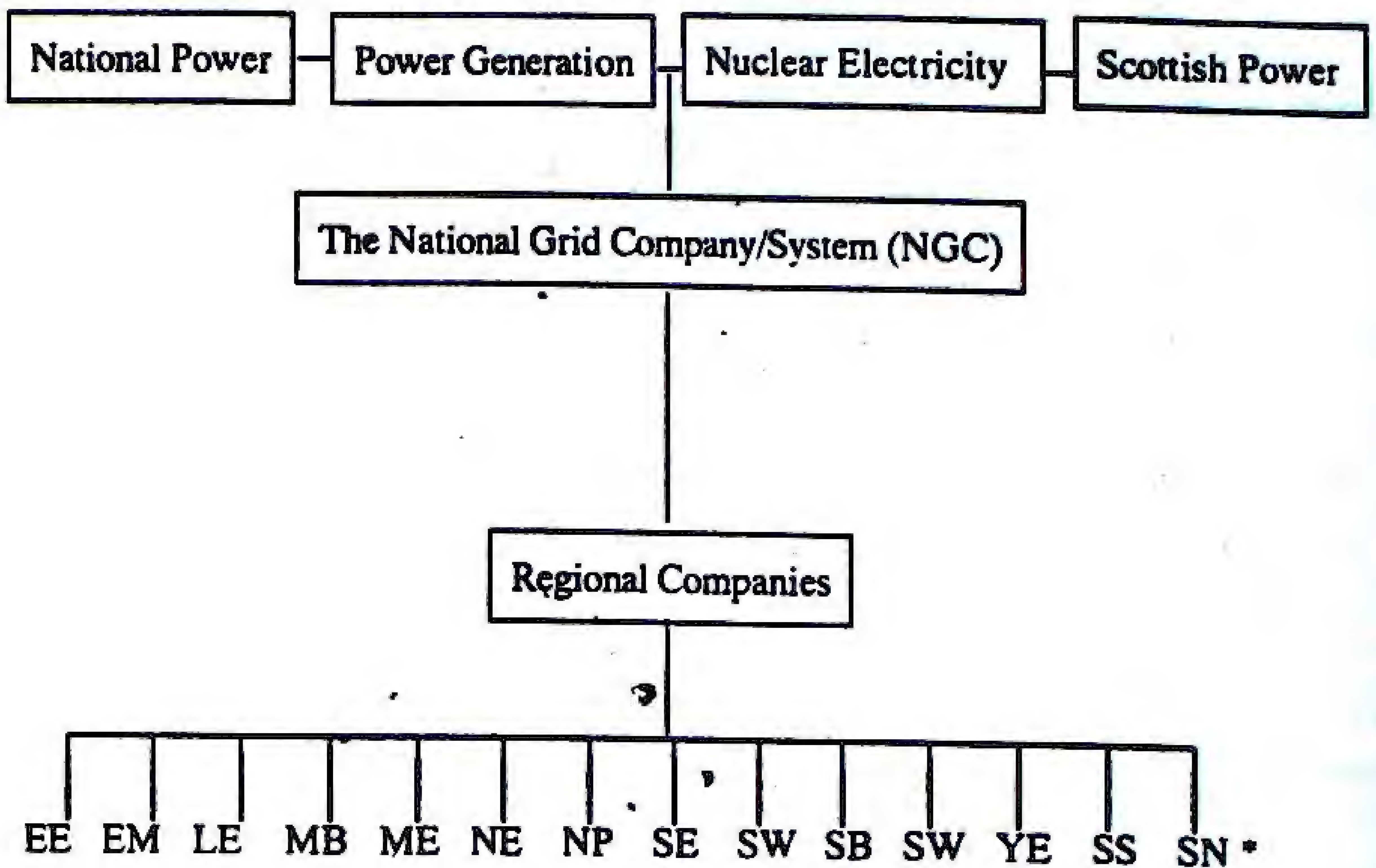
APPENDIX (7.5b)

COMMON SIZE STATEMENT BEFORE CORPORATION

Fixed asset	22644	49%	Equity	43246	93%
Other asset	17049	36%	LT Loans	2403	5%
Current "	6854	15%	St Loans	898	2%
Total Asset	46547	100%	OE&Reser	46547	100%

Source: Data from PTC 1993-94

APPENDIX (8.6)



* name of regional electricity companies

Source: OFFER 1993-1994.

All the above generating companies sell the electricity to the electricity pool via National Grid Company (NGC). The physical flow of the electricity remain the same through the national transmission system. But the NGC and other 14 regional companies have an obligation to offer terms and condition for the use of their system. There is a competition among the RECs and there are different terms and condition regarding these RECs depending on the areas and services regulated and controlled by the regulatory offices.

APPENDIX 8.7

ACID TEST RATIO/LIQUIDITY RATIO: CURRENT ASSETS-STOCKS/CURRENT LIABILITIES

	1992	1991	1990
10679-2,336/1287; 10784-2586/1055 and 6854-1828/898	6.5:1	7.8:1	5.6:1

STOCK HOLDING PERIOD(WEEKS): AVERAGE STOCK/COST OF SALES * 52

	1992	1991	1990
2611/5170*52; 1925/4597*52.and 1263/4242*52	26.30	21.78	15.48

DEBTORS PAYMENT PERIOD (WEEKS): DEBTORS/SALES * 52

	1992	1991	1990
4050/16767*52; 4002/13894*52 and 2951/9954*52	12.60	14.98	15.42

CREDITORS TURNOVER RATIO: Turnovers/Creditors

	1992	1991	1990
16767/1286; 13894/1055 and 9954/898	13.04	13.13	11.08

COMMENTS ON LIQUIDITY RATIOS:

This analysis is a useful measure of the organization's ability to sustain its short term business financial position and to meet the liabilities of the organization when they are due for payments. Generally, liquidity is considered as a short term financial strength and solvency being longer term financial strength of the organization (John Blake 1987, p183). Since conversion to the corporation, the financial position of the Pakistan Telecommunication has become more sound. Before corporation, in 1990, the current ratio was 7.6:1 and after that in 1991, it increased to 10.2:1 and during 1992 it reduced slightly to 8.3:1 due to increase in loans for extension.

The Liquidity position of the T&T department (pre corp) was 5.6:1 in 1990, it increased after corporation to 7.8:1 in 1991 and during 1992 it reached to 6.5:1. This analysis of the organization shows that it made enormous progress especially after the first year of its status change to corporation. No doubt in the second year the PTC could not maintain strong financial position but even than its overall position is too high to the industry average. According to some analysts too high liquidity ratios are not even too good because these can be the cause of the high stocks/inventories as the stock holding period have also been increased. Another cause may be the high debtors/account receivable, for example Pak Telecom has about 13 weeks debtors payment period and this shows that the PTC has some problems with the debt collection.

ANALYSIS OF FINANCIAL STRUCTURE

The Ratios (Rs in m)	1992	1991	1990
Gearing Ratio= Borrowing/Borrowing + Equity * 100			
2797/2797+64761*100 & 2797/2797+58542*100 and 2403/2403+43246*100 =	4.00%	5.00%	5.26%
Debt:Equity Ratio = Total Borrowing/Equity * 100			
4084/64761*100 & 52/58542*100 and 301/43246*100 =	6.31%	6.58%	7.63%
NET WORTH:FIXED ASSETS = Retain Earning/Fixed asset*100			
11597/40736*100, 9297/ 31344*100 and 5412/22644*100=	28.47%	29.67%	23.90%
NET WORTH: TOTAL ASSETS=Retain Earning/Total Assets*100			
11597/68545*100, 9297/62394*100 and 5412/46547*100	16.92%	14.90%	11.63%

ANALYSIS OF FINANCIAL STRUCTURE

The above analysis is quite useful to measure the financial structure of the organization. This can be measured with the help of the Gearing Ratio which measures the degree to which the business is funded by the borrowing rather than by the shareholder equity. Therefore it can be considered in relation to the long term loans as well as the total loans in the business. Some analysts prefer to measure it in relation to the total borrowing to the equity, which is known to debt: equity ratio. The Gearing position of the Pak Telecom is very low which can be a strength or weakness. After conversion of T&T its Gearing went further down by 1% as it is shown in the above analysis. The debt:equity ratio also decreased from

7.63% to 6.31%. In a time of the low profit the company with low gearing is generally considered a safer company; where as in a time of higher profit the gearing up is in the favour of the shareholders because the higher gearing companies can be more attractive to the investors in the time of the higher profit. At the moment, the PTC is enjoying high profit so even higher gearing is not bad for it but on the other hand the lower gearing of PTC shows that the corporation is less risky on the long term which provide the safer investment opportunities to the investors and the other view is that the increased gearing involves increased risks.

This type of situation is explained by John Blake

> *"ratios relating to liquidity, there is no desirable level of gearing, appropriate level will depend on the type of business consideration. The balance to achieved in gearing policy is :*
>
> *(a) On one hand, as long as the return earned on resources financed by the borrowed funds exceeds related interest changes then increased gearing yield benefits to the shareholders.*
>
> *(b) On the other hand, increased gearing involves increased risk"* (John Blake 1987, p189).

According to the above arguments of the John Blake, it is clear that in the country like Pakistan where there are tax holidays from 1990 to 1995 in all new industries and also nominal interest or interest free funds are available for the business, in this type of situation the PTC gearing should be improved rather than reduced to 4% as it is indicated in the above ratios analysis.

THE PRIVATIZATION TRENDS & DEVELOPMENTS IN SOUTH ASIA AND LESSONS FOR FUTURE

By

Mushtaq A. Sajid*

Abstract:- This paper is an analysis and overview of the recent trends and experiences of privatization in Bangladesh, India, Srilanka and Pakistan. The wave of privatization is response to the domestic economic and political situation of these countries. These countries have been adopting the privatization policy in one form or another since the early 1980s. This paper identifies certain social, political and economic constraints in the process of privatization and lessons for year 2000.

Introduction

The privatization policies and programmes are as varied as the countries themselves reflecting the specific characteristics of their circumstances and their economic position. The South Asian developing countries set high goals for privatization e.g. the efficiencies of enterprises would be improved, capital market development would be stimulated, internal and external debt levels would be reduced, the allocation of different resources within the country would be improved, and there is a considerable debate about the fulfilment of these objectives. The sectors and enterprise of different countries have their own unique characteristics that implementation strategies have to vary. However, these countries have vast privatization programme in every field of enterprise.

The recent trend of privatization has been prescribed as a method for improving the operating efficiency and hence profitability of the public enterprises. It is often claimed that the privatised firm will yield a higher return on capital invested and will accelerate economic progress (Gray L. Cowan 1983).

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It is also claimed by some writers and economists that public enterprises are a drain in the public purse and have also failed to meet the social and political objectives set for them. As a result of this there has been growing criticism of public enterprises and their performance in some of these countries. Other policy makers argue that the main cause of poor performance of public enterprises and even of privatized ones in developing countries is poor planning and implementation. Wrong selection of product line, lack of enterprise are seen as the major causes of inefficiency.

Nowadays the governments are gradually trying to eliminate these handicaps or weaknesses as a policy of learning by doing. Alan Rufus Water (1985) states that the present general downward trend in the economic performance of many of the South Asian developing countries and the existence of mass poverty, have increasingly led to the development of strategies for privatization; and foreign investment and private domestic capital are less likely to be regarded as an agents of foreign domination and exploitation. Alan also argues that economic theory is now quite explicit and clear that due to the nature of ownership and hence incentive, a state entity cannot be as efficient as private entity in the production of the same output.

For Water, economic growth in the developing countries can only be achieved through one solution; that is privatization of public enterprises. For him it is self evident that the managers of private enterprises have the incentive to work harder and manage better than the managers of the public enterprises.

It has been suggested that in some developing counties, public enterprises have become a vehicle for corruption, nepotism, misappropriation of the public funds and indeed an instrument for furthering the political and material interests of the ruling parties. Although these are very strong views these things are generally thought to have happened in situations where PEs experience substantial political bureaucratic interference in decision making. The literature reviews show that the public sector enterprises have not been able to achieve their objectives especially in the developing countries. Under these circumstances, the privatization of public enterprises in the developing countries would be justified in order to dispose of the above mentioned problems.

Dinnis A.Rondinelli (1991) also analyzed the rapidly increasing public debts, inadequate revenues and inefficiency of the SOEs in the developing countries by saying that "inadequate revenues and high level of debt service exacerbate the inability of the over-burdned government agencies to provide services and infrastructure efficiently. Many state owned enterprises (SOEs) in the public service industry lose large amounts of money every year, further depleting the government treasury. However, all the above mentioned problems are not attributable only to the state owned enterprises in South Asain countries: they can also be attributabie to poor planning, faulty selection of product lines, underdeveloped infrastructure and undue interference by the governments. If all these handicaps can be removed and SOEs enjoy a competitive environment, then there is no reason that public enterprises can not be successful business entities (Berhanu Mengistu, 1988) Mengistu's arguments seem logical, that if the governments in the developing countries can provide a free and competitive environment while commercializing the state enterprises, then SOEs have the ability to succeed and compete in domestic and international markets.

Privatization in least developed countries was motivated by political as well as economic reasons. Governments' commitments to lower taxes and reduce public sector borrowing requirements, was politically easier to achieve by selling government assets than by cutting expenditure. On the other hand, for economic reasons they wanted to improve efficiency and productivity by introducing competition into the private sector. There are political, historical and ideological reasons behind the privatization movement but economic factors probably are the major one. Another important cause of the privatization movement is the international pressure from the donor agencies to pursue this policy as an economic reform programme.

Implementation Programs in Selected Countries:

The privatization programme was started in the South Asian countries by the influence of the developed countries and objectives according to their social and economic positions. Privatization objectives are, therefore, often more theoretical notions rather than targets for practical implementations. Ideally, there should be a well defined organizational set up and structure within the government to permit orderly and efficient implementation including the prioritization of

candidate enterprises, the definition of responsibilities of outside advisers, and the selection of advisors to monitor the implementation process. Most civil servants are not endowed with either the practical experience or the technical skills required in the implementation proccess. In a few cases, the privatization programme and its objectives are quite clear, but not in most cases. The analysis of the experience in most countries suggests that privatization is proceeding gradually, at best. However, almost all developing countries are divesting state owned enterprises. This wave of Privatization in the developing countries is being done by offering shares publicly on the stock exchange, private sales of shares to domestic or foreign investors, management buy outs and the distribution of shares of vouchers to the general public. It has been to the aim of improving these services and increase their efficiency that the sale of these public enterprises has been directed. Recent developments in privatization in selected Asian countries are discussed as under:

Bangladesh's Experience:

In the early 1970s, after independence, the Bangladesh government nationalized major industries. In July 1974 the government started considering liberalization of state industrial sectors due to the poor performance of the SOEs. By June 1982, a policy was announced to withdraw all restrictions on ceilings for private investment and only 6 industries were reserved for government ownership.

The shift to a policy of economic liberalization after 1975 has included some serious attempts to revive private investment through incentives and disinvestment by the government. Mr Ershad's government was keen to promote manufacturing and pursued a policy reminiscent of early, South Korea and Taiwan. While the industrial capitalist class in the country remains small and lacks of political influence, the government is nevertheless seriously committed to promoting industry, and this is potentially conducive to industrial growth (Clive Hamilton, 1987). The new government has developed its own strategies and public enterprises and defined as public sector corporations and under each of them there are several other units. This sector now consists of 15 financial and 35 non financial enterprises.

Privatization: What & How

The government of Bangladesh has divested a total of 1076 state owned enterprises including 609 in the industrial sector. Most of these divestitures took place during the early 1980s with 33 Jute and 27 textile mills returned to the former owners in 1982. The majority of these units have been transferred to the private sector or negotiated with the former owners and returned to them as part of the denationalization policy.

The government has also decided to carry on gradually the task of restructuring the equity base of state owned enterprises (SOEs) and has undertaken extensive rehabilitation of them. 49% shares of most of SOEs are being sold to private buyers as a part of the gradual privatization process and 15% of these have been given to the workers of the enterprises concerned. The USAID through the Center for privatization and the World Bank under the Structural Adjustment Programme (SAP) have helped the Bangladesh government and also carried out comprehensive privatization studies regarding the industrial and agricultural sectors. With the assistance of the above agencies the government made an evaluation of future privatization opportunities in the country and recommended appropriate strategies for improvement of the privatization programme (Muhith A, 1989). The government has sold most of the manufacturing and agricultural enterprises to the private sector. For example, 50 enterprises under the Bangladesh Chemical Industries Corporation, consisting of 25 tanneries, 5 rubber plants, 7 manufacturing companies, 5 paper manufacturing units and 8 other were sold to the private sector through open bids, and in the Agricultural sector 30 enterprises which came under the Bangladesh Sugar and Food Industries Corporation were also sold to private buyers throuhg open tender for $11.5 million. The following industrial sectors were privatized in the following ways:

Agricultural, chemical industries, textile and Jute mills through private sale; Iron and Steel companies by public shares; machine Tools manufacturing units through management contract.

This privatization programme has been claimed as one of the largest privatization programmes in Asia and has been successful despite some difficulties at different stages of the process. However, the private

investment trend is very low and has hardly improved efficiency except in the textile industries.

Sri-Lankan Experience:

Sri Lankan economic reform started in 1955. The government made a long term plan in 1955 under Government Sponsor Corporation Act 1955, to divest and transfer the statutory bodies into joint stock companies. A 1957 act permitted the government to take over all these joint stock companies. This process was accelerated during 1971 by nationalization of several key private sectors of the industries. The government established various forms of public enterprises, e.g the public companies, government owned companies, the public corporations, government enterprises and government owned business undertakings (David Heald 1989).

In 1977, under the Land Reform Act, some further enterprises were nationalized which meant the country had one of the largest public sectors outside the centrally planned economies. The state owned enterprises (SOEs) accounted for around 40% of the gross output in manufacturing and over 40% of the employment in this sector. Out of 143 state owned enterprises, 127 were from non-financial enterprises and 16 from financial enterprises. They were performing below satisfactory level and so the government decided to improve their position and divest them.

Privatization: What & How

During the 1980s the trend towards privatization was started where a committee was appointed to restructure and improve the efficiency of public sector enterprises. In 1987, the World Bank gave conditional loans to the Sri Lankan government for the divestiture of state owned enterprises and corporations. As a result, the government formed a Presidential committee on the privatization in July 1987 which consisted of high level government officials and the private sector as well. The committee identified 18 enterprises which would be candidates for privatization. The Government has sold some of them and 11 enterprises have been partially divested and 5 enterprises have been contracted out to management. The committee launched an extensive campaign to explain the objectives of the privatization programme along with the economic benefits.

The government endorsed the programme and objectives of the newly formed privatization commission. The rationale, criteria and merits of Privatization have been debated and identified and three main techniques of privatization have been used by the government of Sri Lanka.

The first, complete ownership transfer, has been used in the manufacturing sector, three textile factories have been sold to the private sector. At the time of sale these three factories were profit making units.

Second, partial ownership transfer. The government decided to convert the State Rubber Manufacturing Corporation into a joint stock company, with 60% government ownership and 40% to be offered to the general public and employees. Initially the SRMC position was not good but after the formation of the new company its profits have improved. Third, joint venture and management contract. This approach of full or partial privatization takes advantage of the greater scope for operational autonomy enjoyed by the joint stock companies relative to the public corporations. Under this mode the components of the Bank of Ceylon and Corporative Whole Establishment (CWE) were privatized. Sri Lanka textile companies, Thulhiriya, Pagoda and Vayangoda under the National Textile corporation, Cement Corporation, Kanka Cement, Air Lanka and several Hotels were contracted out (Helon Nankani, 1989 and 1990). However, the Sri Lankan authorities have been careful on the choice of the instruments responding creatively to a multitude of environmental constraints. According to Peter Smith and G Staple (1994), "Sri Lanka has pursued a step by step sector program that has been strongly influenced by other commonwealth countries. The operator, Sri Lanka Telecom (SLT) has been corporatized, the scope for private investment has been broadened, and an independent regulator has been chartered, and all these steps have significantly increased the level and scope of available telecommunications. This is specially so for wireless services: there are now two cellular radio operators, and a third nationwide license is expected (pxxi). This is a new development in the Sri Lankan telecommunications industry. Other industries like National Textile Corporation, Cement corporation and Air Lanka were privatized through management contracts and other enterprises through private sale. The Sri Lankan government experience suggests that the privatization of public utilities required reorganization before the implementation of the privatization process, Sri Lanka Telecommunication department also

provides a good example of the use of complementary sectoral policies in the case of public monopoly. Initial efforts involved formulation of the telecom policy framework, formation of a new legal entity and design of a regulatory body.

Indian Experience:

The Indian government declared a privatization programme in the policy framework of its Seventh Five Year Plan that commenced in 1985, while encouraging overseas investment in certain industries. The industrial policy assigns a more responsible role to private sector which can operate in those areas which were closed to them e.g. telecommunications equipment, power generation and petro-chemicals. (Y. venugopal, 1990). The Indian planning commission has outlined the eighth Five Year Plan, 1990 to 1995, which indicates the selling of 25 precent of state owned enterprises. It is estimated in the plan to raise Rs. 120 billion revenue for the government. According to the new Indian policy joint ventures are welcomed. with a maximum of 49 percent to be held by the government. The government has made further changes, easing the 40% ceiling on foreigners equity holding in Indian companies, allowing Indian companies to raise equity capital abroad, revising monopoly regulation and raising the funds through the privatization programme (K.K Sharma, 1988). The Indian government has made several plans with the help of the USAID but the implementation process is not as fast as in other countries.

Privatization: What & How

The Indian government policy involved, inter-alia, elements of deregulation, liberalization and autonomy to public enterprises in the seventh Five Year Plan, 1985-90. These measures introduced competitive elements into domestic industry and encouraged international direct access to the open market funds, redefining the role of public enterprises. The techniques of contracting out and franchising are not considered as privatization in India, only disinvestment, or divesture is considered as privatization. A greater role was given to the foreign joint venture programme in areas hitherto reserved for public enterprises. The Government of India is using a case by case approach to privatization.

Generally, privatization in India has the following policy and programme:

(a) case by case policy;

(b) deal initially only with loss-making enterprises:

(c) dealing with the competitive sector where the private sector is already dominant:

(d) includes conversion into joint venture.

The Indian government has a great deal of social and equity issues along with those of financial and legal regularity. It is not clear that public enterprises can't improve or that the private sector can be more efficient through the simple transfer of ownership under the current situation. It would however, be unrealistic to proceed on assumption that the issue of Privatization will not take an important place in future economic policy.

The Indian government can show good result if both central and states governments develop combined strategies and policies under a central committee (Ramanadham V.1990). However, in India the pace of privatization and change in the economy depend on the stability of the government because government is facing other problems than the inefficiency of public sector enterprises. For example the burning question is the Political instability in India is also a major cause of slowness of the privatization movement.

Pakistan's Recent Experience:

Despite frequent changes in government, privatization in Pakistan is one of the most important economic reform programmes being implemented in the last 8 years under the leadership of the two major political alliances of the Pakistan Muslim League (IJI) and the Pakistan People's Party (PDA). The most up to date sale of public sector enterprises are as under:

Revenues From Privatization of SOEs During 1991-1996

As PC reported in 1996 (up dated) Rs in millions

Industry/units	Number of Units	Receipts
Automobile	7	1111.91
Cement	11	7648.12
Chemicals	12	1630.49
Fertilizers	1	435.39
Ghee	16	581.93
Rice	8	237.35
Engineering	7	102.49
Roti Plants	12	78.34
Banks	2.	3391.63
Newspapers	5	266.10
Telecom (PTCL)	2(offerings)	30500.0
Others	6	229.39

Source: Privatization commision & Business Recorder (kh)

The above government industrial units were sold during last five years and received about Rs 16260.3 excluding PTCL. The government used pak telecom proceeds for its fiscal operation as provided in original plan (Pakistan Economic Survey 1996).

The consortium of consultants for PTC approved by the IMF has proposed the sale of a controlling stake of 26% and 40% to strategic investors. They will further invest about $5 billion in seven years for expansion of PTCL (The Muslim, December 23, 1996).

An Overview of Privatization Under Various Governments Table-1:

Privatization During Nawaz Sharif's Tenure (1990-93)

Total Units	115
Expected Income	Rs. 300 Billion
No. of units privatised	69
Amount received from sale of 69 units	3.95 Billion
Bank guarantees	Rs. 4.66 Billion
Loans, given to 69 units Written off	Rs. 10.00 Billion
Reserved for golden shake	Rs. 16.35 Billion

Source: The News, Feb, 9, 1996 & Senate Standing Committee.

Table-2:

Privatization During Benazir Bhutto's Tenure (1993-1996)

Total Units	31
No. of units privatised	13
Income after selling units	Rs. 863.9 million
Amount invested for golden hand shake	Rs. 1.00 Billion

Source: The News Feb. 9,1996 & Senate S. Committee.

Table-3:

The privatization: an Overview (1988-1995/96).

Amount Received After Privatization	Rs. 34,531 Billion
Amount Invested on the Social Action Program (SAP).	
Public Sector Development Plan,	Rs. 1600 Billion
Amount Invested on Debt Payment	Rs. 600 Billion

Source: As Above

The above liberalization and privatization development to date shows that different governments have made various programmes for implementation but due to political uncertainity no one could properly achieve its specified goals. As on November 5, 1996 the PPP government was again dissolved and election would be held on February 3, 1997 and newly elected government will take time to establish itself under the current political and economic situation of the country. According to the paper presented on 14-16 December 1996, at PIDE's conference, by A.R. Kamal that Pakistan has been able to privatise 86 manufacturing units. 2 banks, one development financial institution and one thermal unit, 12% shares of PTC and 10% shares of PIA over the last 5 years. While the pace of privatization may have been impressive but it has not been able to realize the avowed objectives. Perhaps the government should draw lessons from its own past privatization experiences as well as from other Asian countries. It is therefore, important to establish the legal framework and its operating mechanism before deregulating monopolistic enterprises/utilities otherwise its consequences may not be favourable.

Pakistan has not yet achieved a continuity and stability in political and economic sector for privatization development. However, the social and physical infrastructure as well as the business environment are gradually developing and if any political group succeeds in ruling for a substantial period of time then Pakistan may have the opportunity to implement a privatization and deregulation policy and to move towards industrialization and self reliance.

Conclusion:

The above analysis of the selected South Asian countries shows that a rapid privatization is taking place especially in regard to the utilities and services sectors i.e. telecommunication, electricity, transportation, education and health care. All these sectors are alleged to be poorly managed by governments which are not able to provide the good facilities and proper standards of service to all consumers. There is thought to be a need for private participation and investment in order to create a competitive environment for the improvement of services and life style leading towards the social, political and economic development of these countries. The comparative studies of above countries and past experiences show that the problem is not one of ownership only. Often there is also a lack of a clear blueprint, organized control, motivation and reward systems and a suitable organizational culture in the above selected Asian countries. These "technical" difficulties may be as constraining as political factors. However, the lessons learned are that the success of any particular privatization project will depend on socio-political development, a well planned infrastructure and an appropriate implementation programme with full political stability and commitment.

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- Public-Private Enterprise Management: A Viable Option.
- Human Resource Management: Concepts & Practices.

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